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Nos. 97-826, 97-829, 97-830, 97-831, 97-1075, 97-1087, 97-1099 and 97-1141

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1997

AT&T CORP., *et al.*, *Petitioners,*

v.

IOWA UTILITIES BOARD, *et al.*, *Respondents.*

GTE MIDWEST INCORPORATED, *Cross-Petitioner,*

v.

FEDERAL COMMUNICATIONS COMMISSION AND THE UNITED STATES OF AMERICA, *Cross-Respondents.*

AND RELATED CASES

On Writs of Certiorari to the United States Court of Appeals for the Eighth Circuit

BRIEF FOR RESPONDENTS THE GTE ENTITIES AND CROSS-PETITIONER GTE MIDWEST INCORPORATED

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May 18, 1998

**The GTE Entities are listed on the inside cover.*

123 pp

The following GTE Entities are respondents:

GTE Service Corporation
GTE Alaska Incorporated
GTE Arkansas Incorporated
GTE California Incorporated
GTE Florida Incorporated
GTE Midwest Incorporated
GTE South Incorporated
GTE Southwest Incorporated
GTE North Incorporated
GTE Northwest Incorporated
GTE Hawaiian Telephone Company Incorporated
GTE West Coast Incorporated
Contel of Minnesota, Inc.
Contel of the South, Inc.

QUESTIONS PRESENTED

1. Did the Court of Appeals correctly decide (i) that the plain terms of the Telecommunications Act of 1996 leave pricing determinations under the local competition provisions of the Act to state public utility commissions, rather than to the FCC; and (ii) that as to both pricing and other intrastate matters addressed by the Act, Section 2(b) of the Communications Act of 1934, 47 U.S.C. § 152(b), limits the FCC's authority to areas where the agency was assigned a role in straightforward and unambiguous terms by Congress?

2. Did the Court of Appeals err in affirming the FCC's determination that the term "network elements" is not limited to equipment in an incumbent's call routing network (and features of such equipment), but rather includes virtually all important aspects of the incumbent telephone company's business, including separate software systems used for business functions (such as billing) and distinct services that are separately available for purchase at wholesale rates?

3. Did the Court of Appeals err in accepting the FCC's determination that in evaluating whether access to a particular network element was "necessary" or whether a failure to provide access to such an element would "impair" an entrant's ability to provide service, *see* 47 U.S.C. § 251(d)(2), the ready availability of alternative facilities outside the incumbent's network should be deemed irrelevant?

4. Did the Court of Appeals err in affirming the FCC's determination that entrants may purchase from an incumbent telephone company *all* of the network elements

QUESTIONS PRESENTED
(continued)

needed to provide service without using any facilities of their own?

5. Did the Court of Appeals correctly interpret 47 U.S.C. § 251(c)(3), which requires incumbent telephone companies to provide network elements to requesting carriers "in a manner that allows requesting carriers to combine such elements," as requiring requesting carriers, rather than incumbents, to undertake the burden of combining elements in order to provide telephone service?

6. Was the Court of Appeals correct in vacating the FCC's rule implementing 47 U.S.C. § 252(I), which provides that an incumbent telephone company must "make available any interconnection, service, or network element provided under an agreement . . . to which it is a party to any other requesting telecommunications carrier upon the same terms and conditions as those provided in the agreement," where the FCC's rule would have allowed requesting carriers to pick and choose individual terms from other agreements without accepting all of the trade-offs that had produced those terms?

RULE 29.6 STATEMENT

Pursuant to Supreme Court Rule 29.6, the GTE Entities advise the Court that each of the GTE Entities listed inside the front cover of this brief is a subsidiary of GTE Corporation. In addition, GTE Corporation has the following subsidiaries or affiliates that have outstanding securities in the hands of the public:

Acentech
AG Communication Systems Corporation
Alabama 1-Franklin RSA Partnership
Anglo-Canadian Telephone Company
BBN Corporation
BC TELECOM, Inc.
Belgacom Directory Services, S.A. (BDS)
Cable-Axion Digitel Inc.
Cable-Axion Quebec Inc.
California RSA No. 4 Limited Partnership
Caribbean Reservation Center, C. por A.
CEIET Continental Telefone S.A.
Chesapeake Directory Sales Company
Communicaciones Telefonicas, C. por A.
Compania Anonima Nacional Telefonos
 de Venezuela (CANTV)
Conagro Telecommunications, S.A.
Continental Telecommunications Company (Nigeria)
Continental Telephone of Saudi Arabia, Ltd.
CTI Compania de Telefonos del Interior S.A.
CTI Holdings, S.A.
CTI Norte Compania de Telefonos del Interior S.A.
Dantel
Danville Cellular Telephone Company Limited Partnership
DELCOM, INC.
Digital Courier International Inc.
Eastern North Carolina Cellular Joint Venture

RULE 29.6 STATEMENT
(continued)

Equicom Systems Management, Inc.
Fayetteville Cellular Telephone Company Limited Partnership
Florida RSA #1B (Naples) Limited Partnership
Fresno MSA Limited Partnership
Gadsden Celltelco Partnership
GTE California Incorporated
GTE CyberTrust Japan Incorporated
GTE Directories (B) SDN.BHD.
GTE Directories Corporation Ltd.
GTE Florida Incorporated
GTE Hawaiian Telephone Company Incorporated
GTE Industries Incorporated
GTE Leasing Corporation
GTE Midwest Incorporated
GTE Mobilnet of Austin Limited Partnership
GTE Mobilnet of California Limited Partnership
GTE Mobilnet of Florence, Alabama Incorporated
GTE Mobilnet of Fort Wayne Limited Partnership
GTE Mobilnet of Indiana Limited Partnership
GTE Mobilnet of Indiana RSA #3 Limited Partnership
GTE Mobilnet of Indiana RSA #6 Limited Partnership
GTE Mobilnet of Jacksonville Incorporated
GTE Mobilnet of Jacksonville II Incorporated
GTE Mobilnet of Ohio Limited Partnership
GTE Mobilnet of Santa Barbara Limited Partnership
GTE Mobilnet of South Texas Limited Partnership
GTE Mobilnet of Terre Haute Limited Partnership
GTE Mobilnet of Texas RSA #11 Limited Partnership
GTE Mobilnet of Texas RSA #16 Limited Partnership
GTE Mobilnet of Texas RSA #17 Limited Partnership
GTE Mobilnet of Texas RSA #21 Limited Partnership
GTE Mobilnet of Wilmington Incorporated
GTE Mobilnet of Wilmington II Incorporated
GTE North Incorporated

RULE 29.6 STATEMENT
(continued)

GTE Northwest Incorporated
GTE South Incorporated
GTE Southwest Incorporated
GTE Sylvania S.A. Electronica,
Quimica, Industrial y Commercial
GTE Telecom Saudi Arabia Ltd.
GTE Yellow Pages Publishing Hungary Kft
Herold Business Data AG
Illinois RSA 1 Limited Partnership
Indiana RSA #1 Limited Partnership
Iowa RSA No. 4 Limited Partnership
Iowa RSA No. 5 Limited Partnership
ISM Information Systems Management (B.C.) Corporation
Jacksonville Cellular Partnership
Kentucky RSA No. 1 Partnership
Knoxville Cellular Telephone Company
La Compagnie de Telephone Anglo-Canadienne/
Anglo-Canadian Telephone Company
Laycon Telecommunications, S.A.
LightStream Incorporated
Mobility Personacom Canada Ltd.
MTX Italia
New Mexico RSA 3 Limited Partnership
New Mexico RSA No. 5 Limited Partnership
New Mexico RSA 6-1 Partnership
Ohio RSA #3 Limited Partnership
Pacific Place Cable Ltd.
Page Saudi Arabia Services, LTD.
Panorama Polska Sp. z.o.o.
Parlance
Parque Industrial ITABO, S.A.
Quebec-Telephone
R.G.B. Technologies Inc.
Radiowealth, Inc.

RULE 29.6 STATEMENT
(continued)

Rapport Interactive Services Inc.
Rockford MSA Limited Partnership
SCM Integrated Systems SDN.BHD
Sherkate Sahami Khass Telephone Sazi Iran
Signa Gateway Corporation
Southern Indiana RSA Limited Partnership
Stentor Resource Centre Inc.
Stentor Services Inc.
Telectronics Financing Corporation
Texas RSA 10B3 Limited Partnership
The Micronesian Telecommunications Corporation
Tuscaloosa Cellular Partnership
VenWorld Telecom, C.A.
Virginia Cellular Limited Partnership
Virginia Cellular Retail Limited Partnership
Virginia RSA 5 Limited Partnership
Virginia RSA 5 Retail Limited Partnership
Wilmington Cellular Partnership
Zona France Las Americas

TABLE OF CONTENTS

Page

TABLE OF CONTENTS
(continued)

TABLE OF CONTENTS
(continued)

Page

TABLE OF CONTENTS
(continued)

Page

TABLE OF AUTHORITIES

Page

Cases

TABLE OF AUTHORITIES
(continued)

TABLE OF AUTHORITIES
(continued)

TABLE OF AUTHORITIES
(continued)

TABLE OF AUTHORITIES
(continued)

TABLE OF AUTHORITIES
(continued)

TABLE OF AUTHORITIES
(continued)

TABLE OF AUTHORITIES
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Page

Miscellaneous

INTRODUCTION

In the Telecommunications Act of 1996 ("Act" or "1996 Act"), Congress established federal standards governing the introduction of competition into markets for local telephone service. The 104th Congress fashioned a specialized mechanism for implementing these standards: private negotiations backed up by arbitrations conducted by state public utility commissions. The Act thus leaves control over implementing the new era of competition in *intra*state markets precisely where control over these markets has always been — in the hands of the States.

The Act also strikes a careful balance. On the one hand, Congress wanted to promote rapid entry by competitors even before they could build ubiquitous local telephone facilities of their own. The Act thus requires an incumbent local telephone company to provide interconnection, wholesale services, and elements of its network to competing entrants. On the other hand, Congress placed equal importance on establishing rules that would (i) encourage new entrants to build facilities; (ii) preserve the traditional goal of ensuring that basic service is universally available at low, affordable rates ("universal service"); and (iii) compensate incumbents fully for the forced use of their networks and services by competitors.

The Federal Communications Commission (FCC), however, attempted to undo Congress's most important decisions. *First*, the FCC sought to usurp authority to set the critical *prices* for wholesale services, interconnection, and network elements, which the Act expressly assigns to the States. *Second*, the FCC radically expanded an incumbent's duty to provide its competitors with access to its network elements in order to promote the FCC's view that it needed to "jump start" entry by new firms. The FCC's rules would have destroyed the Act's careful balance between promoting rapid entry and preserving universal service, compensating incumbents, and fostering true facilities-based competition.

The Eighth Circuit struck down the FCC's most blatant attempts to rewrite the Act and substitute its policy choices for those made by Congress. As we demonstrate below, the Court of Appeals was correct to invalidate the worst of the FCC's usurpations — including its attempt to grab jurisdiction away from the States — but in fact it should have invalidated significantly more of the FCC's Order.

STATEMENT OF THE CASE

A. The Regulatory Background Before 1996.

Regulation of telecommunications has long been divided into separate spheres of responsibility for the States and the federal government. Section 2(b) of the Communications Act of 1934 provides the central command limiting federal authority over intrastate communications. Except for certain enumerated sections of the Act, "nothing in this Act shall be construed to apply or to give the [Federal Communications] Commission jurisdiction with respect to . . . charges, classifications, practices, services, facilities, or regulations for or in connection with intrastate communication service." 47 U.S.C. § 152(b). Regulating intrastate service — including local service — has thus been the exclusive province of state public utility commissions for decades.

Regulators long operated under the assumption that local telephone service is a natural monopoly. State laws thus granted an exclusive franchise in each local service area and provided for regulating the incumbent local exchange carrier (or incumbent "LEC") as a public utility.

The system of exclusive franchises was critical for ensuring that telephone service was universally available at affordable rates to all residents, including those in remote and other expensive-to-serve areas. To promote this objective of "universal service," States set low (often below-cost) rates for basic residential service (particularly in more rural areas) and subsidized those rates with higher, above-cost charges for

business service and for services such as special calling features.[1] It was only by restricting entry into the local market that States could ensure that above-cost rates in some segments of the market would not encourage competitors to enter and strip away the high-margin customers that were funding low residential rates. The exclusive franchise system thus allowed the States to operate a subsidy system by requiring the incumbent carrier to serve as the conduit, or the tax collector, for the subsidy flows, collecting high rates for some services in order to subsidize lower rates for others.

B. The Telecommunications Act of 1996.

In more recent years, advances in technology began to erode the assumption that local service could be provided most efficiently by a single carrier. In the mid-1990s, therefore, many States began efforts to introduce competition into local markets and undertook the difficult task of allowing competitive entry while still preserving the traditional regulatory goal of universal, affordable service.[2]

In the Telecommunications Act of 1996, Congress determined to follow the lead of these States, and concluded that all telecommunications markets should be opened to competition. With respect to markets for local service, Congress rejected the idea that it was efficient for only one

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[1] The FCC has outlined the typical system of implicit cross-subsidies. *See, e.g.*, In the Matter of Federal-State Joint Board on Universal Service, CC Docket No. 96-45, ¶ 11 (May 8, 1997) (hereinafter "Universal Service Order") ("Most states have established local rate levels such that businesses pay more on a per-line basis for basic local service than do residential customers, although the costs of providing business and residential lines are generally the same. In addition, rates charged for vertical services such as touch tone, conference calling and speed dialing, subsidize basic local service rates.").

[2] *See, e.g.*, Cal. Pub. Util. Code § 709 (1994); *see also Iowa Utils. Bd. v. FCC*, 109 F.3d 418, 427 n.7 (8th Cir. 1996).

firm to operate a local network and instead outlined a "pro-competitive, de-regulatory" framework for introducing full, facilities-based competition into all segments of the telecommunications industry. H.R. Conf. Rep. No. 104-458 at 113 (1996) (hereinafter "Conf. Rep."). Congress proceeded explicitly on the assumption that "meaningful facilities-based competition is possible," *id.* at 148, and thus set out to craft a statutory plan that would "accelerate rapidly private sector deployment of advanced telecommunications and information technologies and services . . . by opening all telecommunications markets to competition," *id.* at 113.

To foster the ultimate goal of facilities-based competition, Congress had to strike a careful balance between a series of competing considerations. Congress recognized, for example, "that it is unlikely that competitors will have a fully redundant network in place when they initially offer local service." Conf. Rep. at 148. To spur rapid entry, therefore, Congress allowed competitors to make some use of the existing network facilities of incumbent LECs. But granting access to incumbents' facilities raised countervailing concerns.

First, Congress had to ensure that access to existing equipment was not granted *so* expansively and made *so* attractive that it would stifle incentives for entrants to deploy their own rival facilities. That would sacrifice the long-term objective of the Act (facilities-based competition) in favor of the superficial, short-term achievement of merely multiplying the number of firms in the market using the same network.

Second, Congress had to ensure that incumbents would be fully compensated for the forced use of their property. The bedrock constitutional command embodied in the Takings Clause, U.S. Const. Amend. V, requires that incumbents who are forced to turn over their property to competitors be compensated fully for *all* of their costs and be afforded an opportunity to earn a fair rate of return.

Third, Congress recognized that there was an inherent conflict between competition and the current system of implicit subsidies used to maintain low residential rates. Once markets were opened, cross-subsidies in incumbents' rates would give new entrants an artificial ability to undercut incumbents and to strip away high-value customers. Indeed, by cherry-picking such customers, entrants would divert the very revenue streams that had subsidized below-cost service and would put pressure on the subsidy system to collapse. In confronting this problem, Congress had to protect two goals. First, Congress wanted to preserve universal service. Abandoning universal service altogether and letting the market set rates, after all, would mean *increases* in rates for most Americans. Congress therefore mandated the creation of explicit subsidy funds that would be sustainable in a competitive market. Second, Congress also had to ensure that during the interim period before such new funds were established, States would have sufficient flexibility to ensure that entrants could not cherry-pick the highest-value consumers in the market without making a fair contribution to universal service.

As outlined below, the Act reconciles these competing considerations through a series of restrictions ensuring that each facet of the plan for competition fulfills a limited role and does not upset the structure of the whole.

1. Opening the Local Exchange.

To promote the basic objective of spurring competition, Congress explicitly preempted all state barriers to entry in local service. *See* § 253(a). Congress also recognized that spurring rapid entry would require aiding competitors who would not be able instantly to deploy ubiquitous local networks of their own. Congress therefore imposed a series of duties on incumbents requiring them to allow entrants to use their existing networks.

First, Congress required each incumbent to allow entrants to "interconnect" with its network. *See* § 251(c)(2). This duty

made it possible for an entrant to compete by deploying only a limited network of its own since it eliminated the need to create a free-standing, ubiquitous network that connected all consumers in an area. Interconnection allows an entrant, in effect, to buy ubiquitous access to all consumers on the incumbent's network. Through interconnection, an entrant with only a small network of its own can ensure that customers on its network can speak to everyone else.

Second, Congress acted on its recognition that entrants may need to obtain "*[s]ome* facilities and capabilities (*e.g.*, central office switching)" from incumbents, Conf. Rep. at 148 (emphasis added), by requiring incumbents to make pieces or "elements" of their networks available on an "unbundled basis" in "a manner that allows requesting carriers to combine such elements in order to provide . . . telecommunications service." § 251(c)(3). This provided a method for entrants with *some* facilities of their own to purchase selected pieces of equipment from an incumbent (for example, the "loop" or wire connecting the customer to the switch) so that the entrants could begin competing without having to build out the full facilities needed to serve even a small number of customers.

Third, Congress directed incumbents to make finished telecommunications services available to entrants at wholesale rates. *See* § 251(c)(4). That allowed entrants to provide a limited form of competition by acting as middlemen reselling an incumbent's own service, and more importantly would allow entrants to build up a customer base of significant scale that would then enable them to invest in facilities of their own.[3]

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[3] *Cf.* Remarks of FCC Chairman Reed Hundt, "Antitrust and Interconnection: Old Wine in New Bottles (Telecommunications Act of 1996)," 1996 WL 646783 (November 8, 1996) (explaining that resale played exactly this role as a "competitive stepping stone to facilities-based competition" in long distance markets).

While it granted entrants forced access to incumbents' property, Congress also carefully *limited* these obligations to protect competing objectives served by the Act. In particular, to ensure that access to the existing network would not erode entrants' incentives to deploy competing facilities, Congress carefully circumscribed the duty to provide network elements.

First, Congress defined "network element" as "a facility or equipment used in the provision of a telecommunications service," including the "features, functions, and capabilities that are provided by means of such facility or equipment." 47 U.S.C. § 153(29). Network elements are thus definitionally limited to *physical* parts of the call-routing network — and features provided by those parts.

Second, Congress made it clear that even if a facility qualified as a "network element," a new entrant could not obtain that facility absent some demonstration of need. Congress thus required an evaluation of whether access to a proprietary element was "necessary" for a competitor, and for non-proprietary elements required an evaluation of whether a failure to provide access "would impair the ability of the telecommunications carrier seeking access to provide the services that it seeks to offer." § 251(d)(2).

Through these first two restrictions, Congress limited access to elements to what — as AT&T rightly recognizes — would conventionally be termed "essential facilities" of the local exchange — the facilities that had long been thought to be so difficult to duplicate that they justified treating incumbent LECs as natural monopolies. *See* AT&T Br. 2. These restrictions played a critical role in ensuring that allowing access to existing networks would not undermine the primary goal of "meaningful facilities-based competition,"

Conf. Rep. at 148, by eliminating incentives for entrants to build facilities of their own.[4]

Third, the Act restricted network elements to provide a limited entry path between simple "interconnection," which would be useful only for those who had end-to-end local exchange facilities of their own, and "resale," which would be used by those who had no facilities and who wanted to be middlemen reselling an incumbent's service. By mandating "access" to discrete pieces of the network "at any technically feasible point," § 251(c)(3), Congress provided entrants who had some facilities a method for entering immediately by filling out their networks with leased equipment — but it did not eliminate the need to have *any* facilities whatsoever.

Fourth, Congress directed that incumbents were required to provide these parts of their networks only as separate, discrete pieces — that is, "on an unbundled basis" and "in a manner that allows *requesting carriers* to combine such elements" to provide service. § 251(c)(3) (emphasis added). The statutory rubric of providing "access" to "elements" did *not* require them to turn over their *entire networks* ready for an entrant to use to resell fully preassembled telephone service.

In addition to those limitations on access to network elements, Congress also designed the pricing standards for both network elements and wholesale services to serve the concurrent objectives of retaining incentives for entrants to deploy their own facilities, allowing immediate entry by those who lacked complete networks of their own, compensating incumbents, and preserving universal service.

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[4] *Cf., e.g.*, W. Blumenthal, *Three Vexing Issues Under the Essential Facilities Doctrine: ATM Networks as Illustration*, 58 Antitrust L.J. 855, 860 (1989) ("In light of the potentially perverse competitive incentives created by the opportunity for compulsory access, a plaintiff should not be granted access in an essential facilities case unless the alternatives to the facility are extraordinarily difficult for anyone to put in place.").

Congress required wholesale prices for finished service made available for resale to be based on retail rates reduced only by the "costs that will be avoided by the local exchange carrier" through offering the service at wholesale rather than at retail. § 252(d)(3). That standard ensures that incumbents will be compensated for all their costs (which are necessarily reflected in retail rates set by state regulators) and that entrants who can provide service more cheaply than the incumbent will have an incentive to do so. It also ensures that wholesale rates will incorporate whatever cross-subsidy structure regulators have embedded in retail rates. *Cf.* H.R. Rep. No. 104-204, pt. 1, at 72 (1995) ("The [resale] rate should reflect whether, and to what extent, the local dialtone service is subsidized by other services . . . ."). It thus prevents entrants from purchasing wholesale services without contributing to universal service and ensures that entrants will not be given prices that allow them automatically to undercut the incumbent's rates (which include contributions to universal service).

For interconnection and unbundled network elements, Congress specified that rates must be "based on the cost . . . of providing the interconnection or network element" and "may include a reasonable profit." § 252(d)(1). Properly construed,[5] that standard ensures that incumbents will receive full compensation based on all the actual costs of providing their existing facilities. At the same time, it preserves incentives for entrants to construct their own facilities if they would be more efficient (*i.e.*, lower-cost) than the incumbent's.

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[5] As outlined below, the FCC misinterpreted the standard in § 252(d)(1) to preclude the States from considering either the costs of universal service subsidies or the actual costs of past investments in the network ("historical costs"). *See infra* pp. 15-16. Although the Eighth Circuit vacated that rule on jurisdictional grounds, state commissions have applied a similar interpretation.

2. Reform of Universal Service Subsidies.

Congress also recognized that competition required a comprehensive reform of universal service subsidies. Implicit subsidies embedded in retail rates are not sustainable in a competitive environment. Indeed, if left in place, they would unfairly hobble incumbents in the competitive race. Entrants unfettered by a state-imposed rate structure would have a guaranteed opportunity to offer lower rates than an incumbent. Thus, they could target and strip away precisely the high-margin customers who currently support low residential rates, diverting to themselves the revenues that now fund universal service. That result could not be permitted, since requiring incumbents to continue providing below-cost rates to residential subscribers in that scenario would impermissibly convert the incumbent from a conduit for subsidies to a deep pocket funding the subsidy itself.[6]

Wary of these dangers, Congress demanded reforms in universal service to ensure both that universal service was not sacrificed and that entrants would not be given an unfair advantage by being exempted from universal service burdens. Congress thus commanded in § 254 that the current system of implicit subsidies embedded in rates should be replaced by "explicit" subsidies sustainable in a competitive market. § 254(e).

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[6] The FCC itself has explained that the "system [of implicit subsidies] is not sustainable in its current form in a competitive environment. Implicit subsidies were sustainable in the monopoly environment because some consumers (such as urban business customers) could be charged rates for local exchange and exchange access service that significantly exceeded the cost of providing service, and the rates paid by those customers would implicitly subsidize service provided by the same carrier to others. . . . In a competitive market, a carrier that attempts to charge rates significantly above cost to a class of customers will lose many of those customers to a competitor." Universal Service Order ¶ 17.

Section 254 also makes clear that the States play a critical role in coordinating the transition to a new subsidy structure with the advent of competition. In particular, Congress wanted to ensure that in the interim period before new explicit subsidy systems were fully ready, entrants would not simply be given a free ride by being exempted from any universal service burden whatsoever. Thus, Congress obligated the States in unequivocal terms to ensure that "*[e]very* telecommunications carrier that provides intrastate telecommunications services *shall contribute, on an equitable and nondiscriminatory basis*, in a manner determined by the State to the preservation and advancement of universal service." § 254(f) (emphasis added). No entrant, in other words, could be absolved of a fair share of the burden of universal service. By giving them the flexibility to incorporate universal service costs into the prices for wholesale services and network elements, the Act's pricing standards provided the States a critical ability to coordinate their progress in universal service reform with advancing competition.

3. Decentralized Implementation of the Act.

In opening local markets to competition, Congress was extensively applying federal law to purely *intra*state communications — and particularly to matters of competition in intrastate communications — for the first time. Congress thus faced a significant choice. It could follow the extension of substantive federal law with a corresponding extension in the power of the FCC, or it could rely on a more localized mechanism to implement the Act.

In this deregulatory legislation, the 104th Congress was hardly enamored with the prospect of granting more power to federal bureaucracies, especially in an area traditionally subject to state control. Thus, it should come as no surprise that to implement the Act — part of the stated goal of which was to "reduce regulation," Pub. L. No. 104-104 (preamble) — Congress did not simply turn over the reins to regulators at the

FCC. Instead, Congress pursued a decentralized plan for establishing the Act's "de-regulatory" framework.

First and foremost, Congress did not turn to any government agency at all to administer the Act, but rather relied on *private negotiations* to establish agreements implementing the duties imposed on incumbents. Congress thus imposed a duty on both incumbents and new entrants to negotiate in good faith. *See* § 251(c)(1). Moreover, to provide an incentive for negotiations, the Act freed negotiated agreements from many of the substantive standards of § 251. *See* § 252(a).

Next, Congress provided that if private negotiations proved unfruitful, either party could petition a *state public utility commission* to conduct a binding arbitration on open issues. § 252(b)(1). States thus could use the expertise they had developed through decades as the sole regulators of local service to apply the Act, through individualized arbitration proceedings, to the specific circumstances of particular carriers in different parts of the country while protecting universal service.

In particular, Congress made clear in § 252(d) that *States* would determine the *prices* that would apply to interconnection, unbundled elements, and resold service. That section provides that "a State commission" will make the "[d]etermination" of the rates for interconnection and network elements and spells out the specific standard state commissions are to apply. § 252(d)(1). Similarly, it commands that a "State commission shall determine wholesale rates." § 252(d)(3).

Congress also assigned the FCC a number of significant tasks in implementing the local competition provisions of the Act. If a State decides not to undertake its role under § 252, the statute provides that the FCC "shall assume the responsibility of the State commission . . . with respect to the proceeding or matter." § 252(e)(5). In addition, Congress

assigned the FCC several specific responsibilities, including "exclusive jurisdiction" over "telecommunications numbering." § 251(e)(1). Similarly, Congress envisioned the FCC's having some role in determining which network elements should be made available, *see* § 251(d)(2), and in defining requirements for "number portability," § 251(b)(2).

Significantly, Congress declined to amend § 2(b) of the Communications Act to exempt the new provisions of the 1996 Act from § 2(b)'s strict limitation on the FCC's power over intrastate matters. Indeed, while such an amendment had been part of both the House and Senate bills, *see* S. 652, 104th Cong., 1st Sess. § 101(c)(2) (1995); H.R. 1555, 104th Cong., 1st Sess. § 101(e)(1) (1995), the Conference Committee removed such a provision from the final legislation.

To speed competition, Congress set deadlines for both the States and the FCC. Congress directed the FCC to "establish regulations" for implementing the tasks assigned to it in § 251 "[w]ithin 6 months after the date of enactment,." § 251(d)(1), and directed the States to conclude arbitrations "not later than 9 months after the date on which the local exchange carrier received the request [for negotiations]." § 252(b)(4).

Lastly, consistent with its decentralized approach to administering the Act, Congress provided for exclusive review of state commission arbitration decisions in the various federal district courts. *See* § 252(e)(4), (e)(6). Congress gave the FCC no authority to review the States' determinations.

C. The FCC's First Report and Order.

After passage of the Act in February 1996, private negotiations started promptly and, under timetables set in the Act, state commissions soon began arbitrating agreements. As the Court of Appeals later explained in entering a stay of the FCC's pricing rules, "[t]he Act's system of private negotiation backed by state-run arbitration was operating without the input from the FCC" to speed the transition to competition and had

"initially proved to be successful." *Iowa Utilities Board v. FCC*, 109 F.3d 418, 427-28 (8th Cir. 1996).

On August 8, 1996, however, the FCC issued its 700-page First Report and Order,[7] which threatened to derail that process entirely. While the 1996 Act had set out a self-described "de-regulatory" framework for introducing competition and had carefully limited the expansion of federal regulatory power by assigning a vital role to the States, the FCC's ponderous Order attempted to regulate every facet of the transition to competition and dramatically extended the FCC's authority.

To start, the FCC attempted to countermand Congress's view that private negotiations were a reliable first-line mechanism for implementing the Act. Indeed, the FCC continues to insist that given "disparit[ies] in bargaining power," negotiations could not work unless the FCC declared a "national regulatory baseline" of outcomes to "reduce transaction costs," FCC Br. 10, — *i.e.*, unless the FCC dictated outcomes in advance.

1. The FCC's Proxy Prices and Pricing Rules.

In its First Report and Order, the FCC ignored Congress's fundamental choice to assign the states the authority to implement the Act's pricing standards under §252. The FCC thus declared that *it* had authority to adopt "national pricing rules" and proceeded to relegate the States to the role of mechanically applying detailed methods dictated by the FCC. J.A. 17-18 (¶¶ 104-05). Indeed, while the FCC now portrays its pricing rules as a project in cooperation with the States in which the FCC defined a general "methodology" and the States retained authority to implement that method by setting specific rates, *see* FCC Br. 10, 26-27, the Order went far beyond mere

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[7] In the Matter of Implementation of the Local Competition Provisions in the Telecommunications Act of 1996, CC Docket No. 96-98, 11 F.C.C.R. 15499 (Aug. 8, 1996).

methodologies. The FCC set specific prices — so-called "proxy prices" — that States were *required* to apply unless they justified any departure with a detailed cost study prepared to the FCC's specifications. J.A. 132 (¶ 619).

Not surprisingly, the FCC does not even *mention* its indefensible proxy prices in this Court. In 1996, however, they were a grave threat to the negotiation and arbitration process set out in the Act. By guaranteeing entrants a known price if they held out for arbitrations, the proxies threatened to pull the plug on meaningful negotiations and arbitrations altogether. As the Eighth Circuit explained in entering its stay, "the negotiations preferred by the Congress [were] already breaking down due to the competitors' desire to hold out for the FCC's proxy rates." 109 F.3d at 425.

In addition to setting specific proxy prices, the FCC also spelled out extensive rules that it required the States to follow in implementing the Act's pricing standards. For example, the FCC determined that the cost-based pricing standard for network elements required the States to adhere to the FCC's own newly minted "Total Element Long Run Incremental Cost" or "TELRIC" pricing method. Under that method, network element prices were to be set based only on the forward-looking cost of operating a hypothetical network constructed solely with the most efficient technology available. J.A. 140, 141-42 (¶¶ 685, 690).

The FCC's TELRIC pricing rule would have exposed the States to potentially enormous liabilities, would have undermined universal service, and would have thwarted the goal of facilities-based competition. First, by requiring States to ignore an incumbent LEC's actual investment in its network, the FCC's TELRIC rule would open the States up to potentially massive liability for the taking of LEC property, since the States could not ensure that a LEC would have the opportunity to earn a fair rate of return on state-approved and state-required investments.

Second, the FCC's TELRIC rule would prohibit States from including in the price of network elements the substantial costs of subsidizing universal service. By forcing the States to exclude these subsidy costs from element prices (even before completing universal service reform), the TELRIC rule exacerbated the potential for cherry-picking: new entrants using an incumbent's network elements (with no obligation to serve high-cost residential customers) could selectively capture the high-revenue customers who subsidize universal service and pocket for themselves the revenues that currently fund universal service.

Third, the FCC's TELRIC rule would doom any hope of promoting true facilities-based competition. By making the incumbent's network available at the cost of a hypothetical, least-cost, ideally efficient network, the FCC ensured that no entrant could ever hope to construct cheaper, more efficient facilities of its own, and thus that it would have no incentive even to attempt to do so. The FCC's TELRIC rule aptly reflects the Commission's barely disguised belief that facilities-based competition is not a realistic objective — a guiding assumption to which the FCC clings in its brief in this Court. *See* FCC Br. 5 ("[N]o prospective entrant could hope to compete with the incumbent LECs . . . by replicating the existing local network infrastructure").

The First Report and Order, indeed, was tacitly based on the assumptions that Congress was wrong about the prospect for facilities-based competition in the local exchange, that local service remained a natural monopoly, and that the only way to spur a form of "competition" in local service was effectively to nationalize existing local networks and to sell them off piece-meal so that various competitors could use the same facilities simultaneously to offer the same service under different brand names. Rather than fostering real facilities-based competition, therefore, the FCC set about to generate a form of pseudo-competition by hypothesizing the prices that the process of

competition *might* achieve and declaring by fiat that the existing network should be sold at those prices. In that way, the FCC abandoned the objective of allowing competition to develop so that *competition* itself could gradually drive prices down and sought instead to impose the *end results* of competition through an edict of central planning that would merely promote the proliferation of resellers using the same network — and regulators parceling out rights to use that network.[8]

Finally, the FCC's exhaustively detailed pricing rules eliminated any role for the States other than crunching numbers to implement the FCC's formula. Reducing the States to the function of implementing the FCC's *diktat* was entirely in keeping with the FCC's view of the division of responsibilities in the Act. As the then-Chairman of the FCC put it, in the FCC's view, the 1996 Act threw the State's ability "to make their own decisions on things like local loop unbundling, pricing — that kind of thing" into "the trash can of history."[9] Indeed, to extend its control even further, despite the explicit terms of the Act granting federal district courts exclusive jurisdiction to review state arbitration decisions, the FCC purported to claim that *it* would have authority to review arbitrations under the complaint procedure provided in § 208 of the Communications Act. J.A. 465-69 (¶¶ 121-28).

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[8] *Cf.* Hon. Stephen G. Breyer, *Antitrust, Deregulation, and the Newly Liberated Marketplace*, 75 Calif. L. Rev. 1005, 1018 (1987) (explaining the "special policy risk of deregulation" that regulators may attempt to protect "competitors instead of protecting competition").

[9] Interview with Reed Hundt, *in* Telecommunications Report, Supplement at 10 (July 9, 1996).

2. The FCC's Radical Expansion of the Duty To Provide Unbundled Network Elements.

In addition to seizing control for itself over the Act's pricing terms, the FCC also swung a wrecking ball through each of four critical limitations Congress incorporated into incumbents' duty to provide access to network elements.

First, while Congress had carefully limited the definition of a "network element" to a "facility or equipment used in the provision of a telecommunications service" (or the "features, functions, and capabilities" provided by a facility), § 153(29), the FCC radically expanded the term to include virtually every aspect of an incumbent's business. For example, the FCC concluded that an incumbent must make available to its competitors (i) its operators, (ii) its directory assistance personnel, and (iii) its internal operations support software systems. J.A. 116-17, 129-30 (¶¶ 516, 554). By doing so, the FCC obliterated Congress's effort to restrict elements to what could be considered the "essential facilities" of the incumbent's network.

Second, Congress restricted access even to items that met the definition of "network element" by directing the FCC to consider whether access to proprietary elements was "necessary" and whether failure to provide non-proprietary elements would "impair" an entrant's ability to provide service. § 251(d)(2). The FCC's Order followed a two-step approach to eliminate these limitations. The agency first reinterpreted § 251(c)(3)'s direction concerning *where* incumbents should provide "access" to elements ("at any technically feasible point") into a broad presumption governing *what* parts of the network should be unbundled. It ruled that every element that could technically be unbundled *must* be unbundled. J.A. 49

(¶ 278).[10] Next, when it turned to the restrictions of § 251(d)(2), the FCC sought to protect its erroneous presumption requiring blanket unbundling by reading § 251(d)(2) in a way that would not "significantly diminish the obligation imposed by section 251(c)(3)." *Id.* at 53-54 (¶ 286).

To serve that end, the FCC effectively read the limitations imposed by § 251(d)(2) out of the Act by determining that it would conduct an evaluation of whether access to an element was "necessary," or whether failure to provide the element would "impair" an entrant's ability to provide service, by looking solely to the availability of alternative facilities *within the incumbent LEC's own network*. J.A. 51-52, 54-55 (¶¶ 283, 287). The availability of comparable facilities from other sources (for example, a tandem switch or trunking facilities from a long distance carrier) was irrelevant in the FCC's view. As a result, under the FCC's standard, access to a network element is virtually always required — an incumbent's network rarely contains needlessly duplicative facilities. And since no element would ever be available elsewhere at the price of a hypothetical, most-efficient network (the price mandated by the FCC), buying an element from another source would always "impair" a carrier's ability to provide service.

Third, having expanded the duty to provide "elements" to every conceivable aspect of an incumbent's business, the FCC took the further step of allowing a new entrant to purchase *all* of the network elements needed to provide completed service without providing *any* facilities or personnel of its own. Instead, the new entrant could simply order from the incumbent (at hypothetically most-efficient, cost-based prices) the *entire network* needed to provide completed telephone service, *plus* all of the incumbent's ancillary business functions (such as

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[10] The Court of Appeals struck down this presumption as contrary to the terms of the Act, *see* Pet. App. 46a-47a, and the FCC has not even attempted to seek review of that decision.

operator and directory services) and use all of these so-called "unbundled" elements to provide telephone service. J.A. 59, 63-65 (¶¶ 331, 338-41).

Fourth, the FCC ruled that even though the Act required incumbents only to provide elements in "a manner that allows requesting carriers to combine" them, § 251(c)(3), incumbents would instead be required to provide elements preassembled as they already existed in the network, *see* 47 C.F.R. § 51.315(a), and would even be required to combine them in any new fashion requested by an entrant. *Id.* §§ 51.315(c)-(f).[11]

This quadruple-whammy expansion of the unbundling duty destroyed the careful balance struck by Congress in the Act. By broadening "elements" to include every aspect of an incumbent's business, removing any limit on when they must be provided, and ruling that all elements must be provided already assembled into a functioning platform, the FCC turned network elements into another route for effectively obtaining finished service ready for resale. As a result, an entrant could ignore the statutory terms governing resale and instead could declare that it wanted to use the fiction of ordering *all* of the elements necessary to provide service *preassembled* — and supported by operators, directory assistance services, and operational support systems, to boot. Moreover, an entrant could use this fiction of sham unbundling to evade the wholesale rate under the Act and receive instead a rate that is the sum of the hypothetical, cost-based prices set by the FCC.

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[11] The agency actually attempted an even more extravagant extension of the unbundling duty by declaring that entrants would be able to demand that an incumbent upgrade its facilities to provide them with elements that are "superior in quality to that which the incumbent LEC provides to itself." 47 C.F.R. § 51.311. The FCC thus sought to give entrants the right to control for their own benefit the incumbent's network planning and the deployment of new technology in the network. The Eighth Circuit vacated this rule, *see* Pet. App. 50a-52a, and the FCC has not even attempted to seek review of that decision.

The FCC describes its expansions of unbundling as giving entrants a "choice" about entering the market. On the one hand, the entrant can purchase local service at the Act's wholesale prices — *in which case the entrant would contribute fairly to universal service and compensate the incumbent for the actual costs of its network.* Alternatively, under the fiction of buying "unbundled" elements that are preassembled, the entrant can declare that it wants *all* of the elements needed to provide completed service already combined together into a finished platform — *in which case the entrant would contribute nothing to universal service and compensate the incumbent only for the costs of a hypothetical, ideally-efficient network.*

Far from creating a meaningful "choice" of alternative entry strategies, this end-run around the wholesale rate opened an irresistible avenue for arbitrage that would have upset the careful balances Congress imposed in the statutory pricing standard. It would allow entrants — while merely reselling service provided entirely over an incumbent's network — not only to avoid contributing to universal service, but also to pocket for themselves the revenues from business and urban customers that currently maintain low residential rates. The FCC's rules, in short, would have sacrificed the critical goals of preserving universal service, fully compensating an incumbent for the use of its property, and promoting facilities-based competition, all for the short-term goal of promoting immediate entry by a number of firms and stripping away market share from incumbents.

Not surprisingly, when the Order was released, new entrants could not conceal their glee at this guaranteed opportunity for windfall profits. AT&T's president touted to investment analysts that the network element platform provided new entrants with "another way to resell" incumbent services, but at what he calculated to be a "52 percent" discount from retail rates — more than *two to three times* the discounts set according to the statutory standards for wholesale services.

See Transcript, "AT&T Investment Community Meeting" (March 3, 1997), J.A. 255, 258.

3. The FCC's Pick-and-Choose Rule.

Finally, the FCC distorted the obligation Congress imposed in § 252(i) of the Act. That section requires an incumbent to "make available any interconnection, service, or network element" that it provides under an agreement with one party "to any other requesting telecommunications carrier upon the same terms and conditions as those provided in the agreement." The FCC expanded that unremarkable requirement into an extraordinary option for entrants to pick and choose any individual term from earlier agreements *without* having to accept all the trade-offs and conditions built into the agreement that made those terms possible. J.A. 1044-45, 1048 (¶¶ 1310, 1321).

D. Review in the Eighth Circuit.

Several States, joined by GTE and other incumbent LECs, sought a stay of the FCC's pricing rules and the pick-and-choose rule — the elements of the Order that most immediately threatened to derail the process of negotiations and arbitrations envisioned by Congress. After briefing and oral argument, the Eighth Circuit stayed these provisions.[12]

On the merits, the Eighth Circuit determined that the FCC lacked jurisdiction to issue rules implementing the pricing terms of the local competition provisions of the Act. Centering its analysis on the text of the Act, the court explained that § 252(c)(2) plainly commands state commissions, not the FCC, to establish rates in arbitrations and that § 252(d) again directs

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[12] The FCC, AT&T, and MCI unsuccessfully asked Circuit Justice Thomas to vacate the stay. 117 S. Ct. 378; 117 S. Ct. 379 (1996). The FCC then reapplied to Justice Ginsburg, and AT&T and MCI reapplied to Justice Stevens. After being referred to the Court, these applications were also denied. 117 S. Ct. 429 (1996).

the States to set rates and defines the specific standards they are to apply. Given the absence of any reference to the FCC in the sections of the Act that explicitly addressed pricing, the court concluded that "the Act plainly grants the state commissions, not the FCC, the authority to determine the rates involved in the implementation of the local competition provisions of the Act." Pet. App. 14a.

Alternatively, the court explained that *even if* the text of § 252 were not clear, any ambiguity was resolved by the plain command of § 2(b) of the Communications Act. Under settled law, the restriction of § 2(b) barring the FCC from authority over intrastate matters can be overcome only by a straightforward and unambiguous command from Congress. *See* Pet. App. 15a-19a (citing *Louisiana Pub. Serv. Comm'n v. FCC*, 476 U.S. 355 (1986)). But far from providing any unambiguous grant of authority to the FCC, the 1996 Act unequivocally assigned pricing authority to the States.[13]

Given the command of § 2(b), the court also ruled that the FCC could claim authority to implement other intrastate matters addressed in the Act only where Congress had explicitly given the FCC a role. *See* Pet. App. 12a n.10, 37a.

As to the unbundling rules, the court upheld some of the FCC's decisions and struck down others. The court deferred both to the FCC's view of what constitutes a "network element," Pet. App. 41a-45a, and to the agency's view as to when access to a network element is "necessary" or would "impair" an entrant's ability to provide service, *id.* 47a-48a. The court also agreed with the FCC that the Act did not preclude an entrant from relying *solely* on network elements obtained from an incumbent to provide service. *Id.* 53a-58a.

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[13] Because it struck down the pricing rules on jurisdictional grounds, the court did not address the substantive challenges that GTE and others had brought against the FCC's pricing rules. *See* Pet. App. 23a-24a.

At the same time, however, the court made plain that the Act did not convert network elements into a second avenue for providing the same thing as finished service ready for resale. *Id.* 54a-55a. The court struck down the FCC's rules requiring incumbents to combine elements for new entrants. *See* 47 C.F.R. § 51.315 (c)-(f). In addressing those rules, the court explained that § 251(c)(3) of the Act "unambiguously indicates that requesting carriers will combine the unbundled elements themselves" and "does not require the incumbent LECs to do *all* of the work." *Id.* 53a (emphasis in original). The court further made clear that its "decision requiring the requesting carriers to combine the elements themselves" was critical for preserving the distinction between network elements and wholesale service. *Id.* 56a-57a.

In its initial opinion, however, the court without comment left in place one rule, 47 C.F.R. § 51.315(b), that required incumbent LECs to provide entrants with elements already pre-assembled into a functioning package if the elements were connected in the LEC's own network. In a petition for rehearing, GTE and other parties pointed out that the failure to vacate this rule would undermine the distinction between network elements and wholesale service that the court had recognized as fundamental to the structure of the Act. If an entrant could purchase the network already pre-assembled, it would simply be obtaining finished service for resale, but at a lower price that undermined the system of universal service. The Eighth Circuit agreed and, vacating § 51.315(b), explained that "[t]o permit such an acquisition of already combined elements at cost based rates for unbundled access would obliterate the careful distinctions Congress has drawn in subsections 251(c)(3) and (4) between access to unbundled network elements on the one hand and the purchase at wholesale rates of an incumbent's telecommunications retail services for resale on the other." Pet. App. 71a.

Lastly, the Eighth Circuit struck down the FCC's pick-and-choose rule. Concluding that the terms of § 252(i) in isolation did not flatly foreclose the FCC's interpretation, Pet. App. 25a & n.22, the court proceeded to "'look to the structure and language of the statute as a whole' to determine if the FCC's interpretation of this ambiguous provision is a reasonable one." Pet. App. 25a (quoting *National R.R. Passenger Corp. v. Boston & Maine Corp.*, 503 U.S. 407, 417 (1992)). Under this second prong of *Chevron* analysis, the court held that the pick-and-choose rule would undermine the negotiation process Congress had established, and thus that the FCC's expansive gloss was not a reasonable construction of the Act. *Id.* 25a-27a.

E. The Dialing Parity Decision.

In a decision consolidated for review, the Eighth Circuit applied the same analysis under § 2(b) outlined in its main decision to hold that the FCC's dialing parity rules for *intrastate* calls were beyond the FCC's jurisdiction. *See* Pet. App. 79a-89a.

SUMMARY OF ARGUMENT

1. Congress expressly assigned authority over the pricing terms of the Act's local competition provisions to state public utility commissions. Section 252(c)(2) commands that "State commission[s] shall . . . establish any rates," and § 252(d) provides the standards that States must apply. Neither the FCC's efforts to construct an expansive rulemaking role for itself under the non-pricing terms of § 251, nor its efforts to dragoon into service general grants of rulemaking authority plucked from the 1934 Act can alter the explicit terms of the 1996 Act specifically addressing pricing — all of which direct the States, and only the States, to apply the Act's pricing standards.

Even if § 252 of the Act were not so clear, the Eighth Circuit correctly held that § 2(b) of the Communications Act

confirms the FCC's lack of authority over pricing. Section 2(b) unequivocally commands that ambiguity in the Act cannot be construed to give the FCC jurisdiction with respect to intrastate matters. That directive not only provides a statute-specific rule of construction that defeats any claim for *Chevron* deference to the FCC's grasp for authority over pricing; it also imposes a substantive limit on the FCC's power that can be overcome only by a "straightforward" grant of authority in the Act. No such grant of authority exists here.

2. The FCC's four major expansions of the unbundling duty violate the Act both in their individual terms and in their cumulative effect. First, the FCC stretched the term "network element" to encompass every aspect of a LEC's business, whether or not it formed a part of the call-routing "network." Second, while Congress sought to encourage deployment of competing facilities by requiring an evaluation of need before network elements would be made available, *see* § 251(d)(2), the FCC read this limitation out of the Act. Third, the FCC converted the duty to provide individual pieces of the network into a duty to provide *every* piece, so that an entrant would need no facilities of its own. Finally, the FCC completed its transformation of unbundling by turning an obligation to provide discrete, separate pieces of the network into a duty to turn over the entire network, preassembled into a functioning platform ready to provide service.

This quadruple expansion not only obliterated important distinctions in the Act by making network elements what AT&T has termed "another way to resell," but even worse, it made this second route to resell available at a different price. The FCC provided entrants the irresistible option of relying entirely on the incumbent's network to resell the incumbent's own service, but at a price vastly lower than the wholesale rate set by Congress — a price, indeed, that freed entrants of any of the burdens of universal service. The FCC thus opened an avenue for rampant arbitrage that provided an end-run around

the wholesale rate set by Congress and Congress's repeated commands designed to ensure that competition would not undermine universal service.

The Eighth Circuit rightly recognized that the FCC's approach would "obliterate the careful distinctions Congress has drawn" between network elements and wholesale service, Pet. App. 71a, and properly vacated the FCC's rule requiring incumbents to provide preassembled combinations of elements. But the court also should have struck down the FCC's further three expansions of the unbundling duty.

3. The Eighth Circuit rightly recognized that the FCC's pick-and-choose rule was fundamentally incompatible with Congress's plan for relying on binding negotiations to implement the terms governing local competition. The pick-and-choose rule would have scuttled that plan and made effective negotiations and the creation of binding agreements impossible.

ARGUMENT

I. CONGRESS RESERVED AUTHORITY OVER THE ACT'S PRICING AND OTHER INTRASTATE MATTERS TO THE STATES.

Despite the bold proclamation of the FCC's then-chairman that state control over local competition had been consigned to "the trash can of history," the terms of the 1996 Act reveal an entirely different plan. As the Court of Appeals made clear, proper analysis of the role Congress assigned the FCC in the local competition provisions requires addressing the statute in two steps.

First, even without regard to § 2(b), the Act by its terms unequivocally assigns authority over the pricing provisions of the Act to the States — *not* to the FCC.

Second, reading the Act under § 2(b)'s rule of construction not only confirms that the FCC has no authority over the

pricing terms in the local competition provisions; it also shows that the lower court was correct in limiting the FCC's role in other intrastate matters to subjects where Congress explicitly gave the FCC a role.[14]

A. Congress Expressly Reserved Authority Over the Act's Pricing Provisions to the States.

1. The Plain Terms of the Act Assign Pricing Authority to the States.

Section 252(c)(2) unequivocally provides that in arbitrations "State commission[s] shall . . . establish any rates for interconnection, services, or network elements." Similarly, section 252(d) — the section expressly entitled "Pricing Standards" — makes it clear that "[d]eterminations . . . of the just and reasonable rate[s]" for arbitrated agreements must be made by a "State commission." Section 252(d), moreover, goes on to provide the specific standards that *state commissions* are to apply in determining rates. These provisions make it abundantly clear that the States, not the FCC, are to implement the pricing terms of the Act.

A clear dichotomy in § 252(c) confirms the States' exclusive role in pricing. Section 252(c)(1) generally directs the state commissions in concluding "open issues" in arbitrations to ensure that terms they impose meet *both* "the requirements of section 251" *and* "regulations prescribed by the [FCC] pursuant to section 251." In contrast, the next paragraph specifically addresses *pricing* as a separate matter

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[14] AT&T attempts to slip through the back door some new challenges to the Eighth Circuit's rulings, arguing that the rulings were based on the court's jurisdictional holdings. AT&T Br. 32-34. The Court should not consider these issues, as they were not properly raised in the petitions for *certiorari*. On those issues, the Eighth Circuit did not rule, as AT&T suggests, based on the scope of the FCC's interpretive authority. Instead, the court held that the FCC's actions violated the substantive provisions of the Act. *See* Pet. App. 47a, 52a-53a.

and — omitting any reference to FCC rules — commands solely that States shall "establish rates . . . according to subsection (d)" — *i.e.*, according to § 252(d). As the Court of Appeals explained in staying the FCC's pricing rules, the contrast between subsections (c)(1) and (c)(2) demonstrates that "where Congress intended for the state commissions to follow FCC rules in arbitrations, it expressly said so." 109 F.3d at 424. As to pricing, Congress decidedly did not say so.

The FCC's contrary claim that § 252(c) somehow *supports* its authority over pricing is nonsensical. *See* FCC Br. 27. Under the FCC's tortured reading, § 252(c)(1) covers *all* issues, including rates, and requires States to follow the FCC's rules. Subsection (c)(2) then addresses pricing distinctly, but because pricing was already included in (c)(1), it *adds* a requirement that States also apply the standards of § 252(d). The FCC's interpretation gives no effect to Congress's decision to separate its directions concerning "establish[ing] rates" into a separate subsection. There would have been no need for such a division if Congress had intended all the same directions from § 251(c)(1) to apply to rates. The FCC's reading thus contravenes the settled principle that "[w]here Congress includes particular language in one section of a statute but omits it in another section of the same Act, it is generally presumed that Congress acts intentionally and purposely in the disparate inclusion or exclusion." *Russello v. United States*, 464 U.S. 16, 23 (1983) (citations omitted).

The plain division drawn in § 252(c), moreover, is echoed more broadly in the structure of the Act. Section 252(d) breaks out "Pricing Standards" into a separate, self-contained section that explicitly describes the standards that "State commission[s]" must apply in determining rates and conspicuously omits any role for the FCC.

This special treatment for pricing was no accident. Neither the House nor the Senate bill contained an analog to section 252, but rather in a single section defined the duties imposed

on incumbent LECs and the role that States were to fulfill in arbitrations. In the Senate bill, that section included a broad command for States to ensure that terms imposed in arbitrations "are consistent with the [FCC's] rules." S. 652, 104th Cong., 1st Sess. § 101(a) (creating § 251(d)(5)(D)) (1995). Concerned that such language might be construed to require States to conform to the FCC's commands on all matters, including pricing, States objected to the draft legislation.[15] In response, that language was deleted, a new § 252 outlining the States' role in arbitrations was created, and, in particular, a new § 252(c) established a bifurcated command concerning the standards States were to apply. On matters of pricing, the States were directed to apply solely the standards of § 252(d). The new § 252(d), in turn, outlined the principles for States to use in setting rates.[16] The legislative history thus

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[15] *See, e.g.*, Initial Comments of National Association of Regulatory Utility Commissioners, Implementation of the Local Competition Provisions of the Telecommunications Act of 1996, CC Docket No. 96-88, at 10 (May 16, 1996) (describing States' efforts to influence the Act before the Conference Committee); Comments of the Florida Public Service Commission at 8.

[16] The FCC's supporters would like to dismiss this dramatic restructuring as a non-substantive change. *See, e.g.*, MCI Br. 32-33 & n.23. Indeed, MCI claims that the FCC must retain any role in pricing arguably implied in the House and Senate bills simply because no change was discussed in the Conference Report. *Id.* That approach to the legislative history is insupportable. The plain implications of the reworking of the text cannot be overridden by reference to drafts of the statute. Moreover, MCI's claim that the lack of discussion in the Conference Report can deprive the changed text of any meaning is doubly flawed. It amounts to the view, firmly rejected by this Court, "not only that plain statutory language cannot be credited unless specifically explained in legislative history, but also that the apparent import of legislative history [*i.e.*, the change in text] cannot be credited unless specifically explained in legislative history." *Morales v. Trans World Airlines, Inc.*, 504 U.S. 374, 386 n.2 (1992). In any event, MCI's claim that any substantive change *must* be discussed in the report is flatly undermined

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plainly confirms what the text of the Act makes clear: Congress expressly singled out pricing and reserved it to state control.

2. The FCC Cannot Point to Any Terms in the 1996 Act Assigning It Authority Over Pricing.

In the face of § 252's express assignment of pricing authority to the States, the FCC cannot point to any language that plausibly supports its claim to a role in pricing. Indeed, the FCC meticulously avoids § 252 — the section that explicitly addresses pricing — and diverts attention instead to § 251.

Specifically, the FCC claims that § 251(d)(1) gives it plenary rulemaking authority to implement "this section" and that this power extends to pricing. *See* FCC Br. 18. *See also* MCI Br. 27. That argument is flawed in several respects. In the first place, as the Eighth Circuit recognized, § 251(d)(1) is not a grant of rulemaking authority. Rather, it places a limitation on the FCC by directing the agency to complete "[w]ithin 6 months after the date of enactment" any rulemaking in areas where it has power under § 251.

Second, even if § 251(d)(1) could imply authority for the FCC to implement the terms of *that section*, as the court pointed out, "[n]owhere in section 251 is the FCC authorized specifically to issue rules governing the rates" for local competition. Pet. App. 12a. The pricing standards of the Act appear in § 252, not § 251.

To fill that hole, the FCC seizes upon the fact that in defining the duties imposed on incumbents, § 251(c) mentions

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[16] (...continued)
by the preamble to the report itself, which makes clear that in addition to omitting discussion of "clerical corrections" and "minor drafting" changes, the report also does not discuss "conforming changes *made necessary by agreements reached by the conferees*." Conf. Rep. at 113 (emphasis added).

"just" and "reasonable" "rates, terms, and conditions" for interconnection and network elements and "wholesale rates" for services. *See* § 251(c)(2)(D), (c)(3), (c)(4)(A). According to the FCC, § 251(d)(1) gives it authority to "implement" § 251(c)'s references to rates. FCC Br. 18. The FCC thus proceeds with its eyes shut tightly to the plain terms of the statute, pretending that § 251(c) sets out the "substantive rate provisions" of the Act. *Id.* at 28. That is fanciful. Section 252 expressly defines the "Pricing Standards" of the Act, and the plain terms of both § 251 and § 252 make clear that Congress directed the States to implement those standards.

Indeed, even § 251(c)'s passing reference to "just" and "reasonable" rates itself directs that this duty should be implemented "*in accordance with*" the "requirements" of "*section 252.*" § 251(c)(3) (emphasis added). Section 252(c)(2) in turn directs the States to set rates following only the standards of § 252(d). Section 252(d), in fact, is the *only* section in the Act in which Congress defined the standards of "just and reasonable" rates and "wholesale" rates mentioned in § 251(c). Moreover, if there were any doubt that § 252(d) is the controlling provision on authority over pricing, § 252(d) states plainly that the States have the role of defining "just and reasonable rates" "*for purposes of*" the duty imposed in § 251(c). § 252(d)(1) (emphasis added). *See also* § 252(d)(3) ("*For the purposes of section 251(c)(4)*, a State commission shall determine wholesale rates . . . .") (emphasis added).

The FCC's claim that the relationship runs the other way, *see* FCC Br. 28 n.10, and that § 251(c)'s reference to § 252 somehow gives the FCC plenary authority to promulgate rules implementing § 252 — a section that conspicuously makes no mention of the FCC — ignores the terms of the Act. Congress directed that "*for purposes of*" any reference to rates in § 251, *state commissions* would determine rates under the standards defined in § 252. *See* § 252(d)(1), (3) (emphasis added). Congress could hardly have used any clearer language to

establish that to the extent rates were mentioned in § 251, the task of implementing the Act's *rate* requirements was to be carved out and implemented solely through the explicit commands given to the States in § 252.[17]

3. The FCC's Second-Line Statutory Arguments Provide No Better Support for Its Claim to Pricing Authority.

Unable to construct a coherent argument for its claimed pricing authority based on the express commands of the 1996 Act, the FCC and its supporters comb through both the Communications Act of 1934 and additional provisions of the 1996 Act hoping to find snippets to bolster the FCC's claims. To start, the FCC seizes upon a grab-bag of general provisions from the 1934 Act that grant the agency rulemaking power and tries to press them into service for its pricing authority under the 1996 Act. Specifically, the FCC calls upon §§ 201(b), 303(r) and 154(i), but none is up to the task.

Despite the FCC's protests, the Eighth Circuit rightly held that § 201(b) is limited to *interstate* communication. *See* Pet. App. 12a. Section 201(a) addresses solely "interstate or foreign communication by wire or radio," and the first sentence of § 201(b) limits that section to "*such* communication service." (emphasis added). AT&T's assertion that the subsequent "sentences" of the section are somehow not limited to interstate communication is preposterous. *See* AT&T Br. 23-24. The next clauses (they are not separate sentences at all) are merely provisos limiting the duty applied to "such

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[17] The FCC's tortured construction, moreover, does not even apply to pricing for wholesale service. The FCC's textual link — the reference in § 251(c) to rates "in accordance with . . . section 252" — does not exist in § 251(c)(4). Rather, the only cross-reference is § 252(d)(3)'s command that "[f]or the purposes of section 251(c)(4), a State commission shall determine wholesale rates." This hole in the FCC's theory confirms that the FCC has the relationship between the sections backwards.

communication service" in the first sentence. They imply no departure from the basic subject matter of interstate communication. In any event, even if the last sentence of the section were somehow wholly unconstrained by the context preceding it, the FCC cannot pluck such a generalized term out of the 1934 Act and purport to trump the 1996 Act's express grant of exclusive authority over pricing to the States. As this Court has repeatedly affirmed, "it is a commonplace of statutory construction that the specific governs the general." *Morales v. Trans World Airlines, Inc.*, 504 U.S. 374, 384-85 (1992) (citation omitted).

For the same reason, the general rulemaking provisions of § 303(r) (which appears only in a list of FCC responsibilities relating to *radio* communications) and § 154(i) (which is simply the general grant of power to the FCC to execute "its functions" assigned elsewhere under the Act) cannot support the FCC's claims. Indeed, these provisions are particularly poor candidates for trumping § 252's explicit directions assigning pricing to the States since each is expressly limited to grant power only to the extent consistent with other provisions of the chapter.[18]

The FCC next runs through a list of provisions in the 1996 Act that it claims can bolster its assertion of pricing authority. In each case, the argument is the same. According to the FCC, these sections obliquely acknowledge a role for the FCC in implementing intrastate matters but do not *expressly* grant the FCC rulemaking power. In the FCC's view, therefore, one or another of the provisions in its grab-bag should be stretched to

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[18] *See* 47 U.S.C. § 303(r) ("*Except as otherwise provided in this chapter*, the [FCC] . . . shall . . . make such rules and regulations . . . not inconsistent with law, as may be necessary to carry out the provisions of this chapter . . . .") (emphasis added); *id.* § 154(i) ("The [FCC] may perform any and all acts, make such rules and regulations, and issue such orders, *not inconsistent with this chapter*, as may be necessary in the execution of its functions.") (emphasis added).

supply it with a broad authority to implement *all* local competition provisions of the Act, including the pricing terms, in order to avoid the "interpretive anomalies" that might result if some sections *acknowledged* a rulemaking role for the FCC without some other section *expressly granting* that role. FCC Br. 21. But an oblique reference to a role for the FCC on one topic cannot justify expanding general or ambiguous phrasing in *another section* so as to trump the explicit assignment of pricing authority to the States in § 252. Moreover, as outlined below, none of the provisions the FCC cites even implies the broad-ranging role the FCC would like.

The FCC first relies on § 251(d)(2), which outlines the standards that the FCC must apply in determining what network elements should be unbundled. While the section does expressly indicate a role for the FCC in implementing the unbundling obligation under the Act, that hardly indicates any broader role for the agency, particularly any role in pricing. To the contrary, the section strikingly demonstrates that where Congress intended the FCC to play a rulemaking role, Congress recognized that role explicitly in the text and prescribed standards for the FCC to apply.

Next, the FCC would rely on § 251(d)(3). *See* FCC Br. 22-23. That section, however, in no way assumes a broad rulemaking role for the FCC. To the contrary, as its title — "Preservation of State Access Regulations" — suggests, it assumes power in the *States* to define access requirements and explicitly *limits* the FCC, directing that the FCC "shall not" preclude the enforcement of any state access rules that are "consistent with the requirements of this section" and that do not "substantially prevent" implementation of the "requirements of this section" and "purposes of this part." § 251(d)(3). The FCC's attempt to suggest that the reference to "purposes of this part" implies a broad-ranging role for it in defining extra-textual "purposes" of the Act simply distorts the text. The clear import of the section is to require the FCC to

hew closely to the terms of the statute in order to prevent the agency from intruding on States' rules more than required to implement Congress's commands. Moreover, once again, it is particularly fanciful for the FCC to argue that a limitation on its power over one subject — access rules — can be transformed through negative implication into a sweeping grant of authority over a different subject — pricing.

Reaching to increasingly remote sections of the Act, the FCC next points to § 253(d), which gives the FCC a circumscribed authority "after notice and an opportunity for public comment" to preempt state laws that are the most egregious obstacle to the Act, namely those that flatly "*prohibit* or have the effect of *prohibiting*" any entity from providing a telecommunications service. § 253(d) (emphasis added). Contrary to the FCC's implausible assertions, that limited ability is not a blank check for the FCC to promulgate rules promoting its self-aggrandizing regulatory agenda. Rather, the section expressly allows the FCC to act only retrospectively after a "State or local government has permitted or imposed" a legal requirement prohibiting entry.

The FCC's appeal to § 160, which the Eighth Circuit ruled was not even properly raised below, *see* Pet. App. 13a n.11, is equally unavailing. That section was part of a separate title addressing "Regulatory Reform." It allows the FCC to forbear from enforcing any provision of the entire Communications Act and requires the agency before doing so to consider whether "charges, practices, classifications, or regulations" will be "just and reasonable," § 160(a)(1). It also restricts the FCC's ability to "forbear from applying the requirements of section 251(c)." § 160(d). From this, the FCC again jumps to the conclusion that any time it is mentioned in the same sentence as the word "rates" or "charges," Congress must have given it plenary authority specifically to implement § 252(d), and that it must have authority over § 251(c) as well.

Such inferences are wholly unwarranted. Since § 160 applies to the entire Communications Act, it had to refer to "charges" to ensure that the new regulatory forbearance measure would apply to all the charges for interstate service that the FCC has long controlled. Moreover, even in the 1996 Act, the FCC has an *express* role in implementing *some* unbundling provisions of § 251(c), *see* § 251(d)(2), and an explicit role in applying both the Act's pricing terms and § 251(c) when a State refuses to conduct arbitrations. *See* § 252(e)(5). The terms of § 160 thus mesh comfortably with the terms of both the 1996 Act and the 1934 Act without any need to invent an *über*-rulemaking authority for the FCC.

Lastly, the FCC strains to pluck pricing authority out of its entirely unrelated role in certifying Bell Operating Company (BOC) compliance with the competitive checklist that regulates BOCs' admission into the long distance market. *See* FCC Br. 29-31. The checklist requires a BOC to offer interconnection and network elements in accordance with the requirements of § 251(c) and § 252(d)(1), *see* § 271(c)(2)(B), and directs the FCC to approve an application only if "it finds that . . . [the BOC] has fully implemented the competitive checklist." § 271(d)(3)(A)(i). The FCC's theory that it cannot possibly determine compliance with § 252(d) unless it has independent authority to define the standards of that section is fanciful. Section 271 does not give the FCC any independent role in pricing; it does nothing more than require the FCC to ensure that a BOC has complied with what § 252(d)(1) calls for — namely, the "[d]eterminations *by a State commission* of the just and reasonable rate" for interconnection and elements. § 252(d)(1) (emphasis added). The FCC's effort to turn the statute around ignores once again the maxim that the specific governs the general. A mere cross-reference to § 252(d)(1) cannot *negate* the explicit command in § 252(d) for the States to establish rates and *reassign* authority to the FCC.

The FCC's effort to twist § 271 into authority over pricing is particularly audacious, moreover, since Congress recognized that control over the BOCs' gateway into the long distance market would give the FCC a potential choke-hold on the companies and explicitly directed the FCC not to stray from the text of the Act. Congress thus commanded that the FCC "may not, by rule or otherwise, limit or extend the terms used in the competitive checklist." § 271(d)(4). The FCC's attempt to parlay the mere cross-reference to § 252(d)(1) into complete rulemaking authority over pricing would accomplish precisely the sort of expansion of power that Congress forbade.

4. The FCC's Policy Arguments Ignore Congress's Plan for Implementing the Act and Cannot Override the Text of the Statute.

Having failed to provide any textual basis for its authority over pricing, the FCC and its supporters predictably resort to a host of policy arguments. The FCC tries to reconcile its assertion of power with the terms of the Act by arguing that it has not usurped the States' pricing role *entirely*. Rather, the FCC claims, it has devised a system of "concurrent and complementary pricing roles" under which the FCC prescribes pricing methodologies and the States set actual rates. FCC Br. 26; *see also* MCI Br. 30-31. This effort to justify the FCC's approach is also fatally flawed.

In the first place, the First Report and Order did not limit the FCC to this newly-packaged cooperative role at all. Rather, it set specific proxy prices that States were required to apply. J.A. 132 (¶ 619). Not surprisingly, even the FCC does not defend its improper attempt to set specific rates in this Court.

Moreover, the FCC's current embrace of a "cooperative" role is nothing more than patronizing rhetoric. The FCC pays lip-service to the idea of reserving to the States the "important task of tailoring [the Act's] standards to accommodate region- or carrier-specific variables," FCC Br. 39, and allowing States

to "exercise their considerable discretion," *id.* at 26, because the text and structure of the statute amply reveal Congress's intent to enlist the expertise of States in administering the Act and in particular to rely on their judgment in making "[d]eterminations . . . of the just and reasonable rate." § 252(d)(1). But after the FCC has exhaustively defined and artificially restricted the costs state commissions are allowed to consider, it leaves the States no role other than plugging numbers into a uniform FCC formula.

Finally, the dual control over pricing that the FCC espouses has no basis in the text of the Act. As outlined above, the Act's pricing terms are directed to the States and only to the States — they suggest *no* role for the FCC at any level of generality. Indeed, § 252(d) explicitly defines the "Pricing Standards" that are to be used to set rates and directs the *state commissions* to implement them. Seeking a textual hook for its argument, MCI suggests that the command to the States to "establish" rates somehow limits the States' role and distinguishes their function from the broader one of "prescribing pricing methodology." MCI Br. 30. But that purported distinction is baseless. Far from suggesting a narrow role for the States, Congress made it perfectly clear that it expected them to exercise considerable discretion by directing them to make "*[d]eterminations*" of "just and reasonable rate[s]." § 252(d)(1) (emphasis added).

The FCC's strained attempt to support its theory of dual pricing roles is particularly unconvincing since the terms of the 1996 Act bear no resemblance to other statutes clearly granting the FCC the role it longs for here. For example, in the Cable Act of 1992 — which the FCC itself showcased below as an example of the sort of role it has in mind — Congress explicitly directed that "[t]he Commission shall, by regulation, ensure that [cable] rates . . . are reasonable," 47 U.S.C. § 543(b)(1), and enumerated specific "factors" the FCC was to consider, § 543(b)(2). Congress also left no uncertainty about

the States' subsidiary role in applying the FCC's determinations as it directed that "the rates for the provision of basic cable service shall be subject to regulation by a franchising authority . . . in accordance with the regulations prescribed by the Commission." § 543(a)(2)(A). Even a cursory comparison to the Cable Act amply demonstrates that Congress knew how to create a system of dual authority over pricing and that it simply did not take that approach in the 1996 Act.[19]

Next, the FCC and its supporters fall back on a parade of horribles they claim will result from the decision below. Their dire warnings boil down to the repeated assertion that the Eighth Circuit has supposedly created an "incoherent jurisdictional scheme," MCI Br. 35, in which States will be applying "radically disparate methodologies" to pricing, FCC Br. 30, and in which there will be endless rounds of litigation before the courts ever arrive at what the FCC's rules already provide: a single, uniform, nationwide interpretation of the finest details of the pricing methods to be used under the Act.

What the FCC and its supporters attempt to caricature as a descent into chaos, however, is nothing more than a system that allows the States much-needed localized discretion in applying the federal standards supplied by the Act — an outcome the 104th Congress saw as one of the *advantages* of federalism. The FCC's strident claims that States will be wildly varying on basic methodological issues is belied by the

[19] AT&T's claim that this Court found such a plan for dual control over rates under the Medicaid Act despite supposedly clearer language assigning responsibility to the States is simply false. *See* AT&T Br. 26 (citing *Wilder v. Virginia Hospital Ass'n*, 496 U.S. 498 (1990)). *Wilder* involved no question of the agency's authority, but addressed only the availability of a § 1983 action. The statute, moreover, made the agency's oversight authority clear as it required States to "mak[e] assurances *satisfactory to the Secretary [of HHS]*" that the rates they used were "reasonable and adequate." *Id.* at 503 (quoting statute) (emphasis added).

terms of the Act itself. Section 252(d) provides sufficient guidance to ensure that States will operate under the same fundamentai principles. And while it is true that application of the Act's standards may vary in the details from State to State, it is entirely appropriate for different States to take into account their particular regulatory histories and current circumstances by considering different categories of costs in setting rates.

Two obvious circumstances that would vary from State to State and that States would have to accommodate in setting rates involve the ever-important issues of protecting universal service and compensating incumbents for their historical investments. By assigning the States control over pricing, Congress ensured that the same entity that controlled both the level of intrastate universal service subsidy costs and the mandated investments incumbents must make in their networks would also have authority to set prices for use of the incumbent's property that would fairly distribute those costs.

B. Section 2(b) Independently Confirms That the FCC Has No Jurisdiction Over Pricing, and Also Restricts the FCC's Authority Over Other Intrastate Matters Addressed by the 1996 Act.

As outlined above, the Court of Appeals squarely held that "the Act plainly grants the state commissions, not the FCC, the authority to determine the rates involved in the implementation of the local competition provisions of the Act." Pet. App. 14a. It went on, moreover, to buttress that holding by ruling that even if the Act were ambiguous in assigning pricing to the States, "[a]ny ambiguity regarding the FCC's vacuum of authority over local telecommunications pricing under the Act is resolved by operation of section 2(b)" *against* the FCC. *Id.* at 15a.

Because the Court of Appeals was correct that the Act explicitly assigns pricing authority to the States, whether or not § 2(b) applies does not matter for the question of authority over

pricing. Nevertheless, the court's § 2(b) analysis is correct, and provides an *independent* ground for invalidating the FCC's assertion of jurisdiction over pricing. Section 2(b), moreover, provides the critical command limiting the FCC's authority over other, non-price intrastate matters addressed in the Act.

1. Section 2(b) Is a Statute-Specific Counter-*Chevron* Rule of Construction.

Section 2(b) of the Communications Act of 1934 unambiguously commands that "nothing in this Chapter shall be construed to apply *or to give the Commission jurisdiction with respect to* . . . charges, classifications, practices, services, facilities, or regulations for or in connection with intrastate communication service." 47 U.S.C. § 152(b) (emphasis added). As this Court has explained, the section constitutes a "congressional denial of power to the FCC." *Louisiana Public Serv. Comm'n v. FCC*, 476 U.S. 355, 374 (1986). Indeed, the court has emphasized that the "sweeping" wording of the section "[b]y its terms" "fences off from FCC reach or regulation intrastate matters — indeed, including matters 'in connection with' intrastate service." *Id.* at 370.

In addition, § 2(b) "provides its own rule of statutory construction," *id.* at 377 n.5, under which any ambiguity concerning the application of the statute or the extension of FCC jurisdiction over intrastate matters must be resolved *against* extension of federal authority. Section 2(b) thus provides a statute-specific, counter-*Chevron* rule that precludes the FCC from claiming deference for attempts to extend its rules to intrastate matters. *Cf. Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837, 842-43 (1984).

This rule of construction, moreover, plainly applies to the local competition provisions of the 1996 Act. Indeed, Congress pointedly *declined* to amend § 2(b) to exempt the local competition provisions from its reach. While both the House and Senate bills included such an amendment,

see S. 652, 104th Cong., 1st Sess. § 101(c)(2) (1995); H.R. 1555, 104th Cong., 1st Sess. § 101(e)(1) (1995), Congress *removed* such a provision from the final legislation.[20]

2. The Court of Appeals Correctly Held That Section 2(b) Would Resolve Any Ambiguity in the Act Against the FCC's Assertion of Jurisdiction Over Pricing Matters.

As the Court of Appeals correctly concluded, even if the Act were ambiguous in assigning pricing jurisdiction to the States — which it is not — § 2(b) would resolve that ambiguity against the FCC's assertion of jurisdiction.

As the Court of Appeals found, "the prices that incumbent local exchange carriers may charge their new competitors for interconnection, unbundled access, and resale ... as well as the rates for the transport and termination of telecommunication traffic qualify as 'charges . . . for or in connection with intrastate communications service.'" Pet. App. 15a. Accordingly, the rule of construction embodied in § 2(b) applies, which means that the FCC has no jurisdiction over prices unless the Act "unambiguous[ly]" and "straightforward[ly]" gives it such jurisdiction. *Louisiana*, 476 U.S. at 377. Even if one were to disagree with the Court of Appeals' primary holding that the Act "plainly" assigns pricing jurisdiction to the States, Pet. App. at 14a, the Act cannot be fairly characterized as doing the opposite — namely, "unambiguous[ly]" and "straightforward[ly]" assigning pricing jurisdiction to the FCC. Accordingly, under the rule of

[20] The FCC attempts to bury this damning fact in a footnote and to dismiss the elimination of the amendment as a "non-substantive" change because it was not expressly discussed in the Conference Report. But that tactic ignores the express statement in the Report that it does not discuss "conforming changes made necessary by agreements reached by the conferees." Conf. Rep. at 113. *See also supra* n. 16.

construction in § 2(b), any ambiguity is resolved *against* the FCC's assertion of jurisdiction.

The FCC and its supporters offer four insubstantial arguments to avoid this straightforward application of § 2(b).

First, the FCC dredges up the same list of supposed "interpretive anomalies" addressed above, *see supra* pp. 34-35, to argue that the Act must be read to grant it broad powers over *intra*state matters relating to both pricing and nonpricing issues. As explained earlier, none of the provisions to which the FCC points implies any broad rulemaking power for the FCC whatsoever. But more importantly, the FCC's entire approach to establishing its supposedly "straightforward" grant of jurisdiction is precisely what § 2(b) *prohibits*. The FCC's entire argument is an effort to pick out sections of the Act that the FCC thinks *obliquely* suggest some rulemaking role for it and to leverage these sections into a basis for "constru[ing]" *other* ambiguous or general provisions of the Act into a sweeping grant of rulemaking authority over *all* intrastate matters. That roundabout approach to the text is exactly what does *not* provide a "straightforward" and "unambiguous" command sufficient to "override" § 2(b). *Louisiana*, 476 U.S. at 377.

Indeed, where Congress has intended to supersede § 2(b) by expressly assigning the FCC intrastate authority, it has generally done so in exceedingly clear terms. In the 1996 Act itself, for example, Congress directed that the FCC should "take all actions necessary" to "prescribe regulations that establish a per call compensation plan . . . for each and every completed *intrastate and interstate call using [a] payphone*." § 276(b)(1)(A) (emphasis added). Similarly, in § 225, Congress directed the FCC to "ensure that *interstate and intrastate* telecommunications relay services are available . . . to hearing-impaired and speech-impaired individuals." § 225(b)(1) (emphasis added). Congress thus demonstrated repeatedly that it could provide exactly the sort of

unambiguous command that would override § 2(b); yet the FCC can nowhere point to remotely comparable language giving it any role in pricing for the local competition provisions.

Second, the FCC and other petitioners attempt to circumvent § 2(b) by arguing that the 1996 Act straightforwardly *applies* to intrastate matters, and that this alone should suffice to give the FCC rulemaking power. That approach runs afoul of the plain terms of the section, which expressly imposes a *dual* limitation — phrased in the disjunctive — commanding that "nothing in this Chapter shall be construed *to apply or to give the [FCC] jurisdiction with respect to*" intrastate matters. 47 U.S.C. § 152(b) (emphasis added). According to the FCC, however, the disjunctive phrasing should simply be ignored.

On this score, the FCC's primary argument amounts to the assertion that federal telecommunications law cannot conceivably apply to any matter outside the FCC's rulemaking authority. The FCC argues this proposition: as long as the Communications Act applied only to interstate matters, the FCC's jurisdiction was coextensive with the Act; therefore, now that the Act also applies to intrastate matters, the FCC's authority should automatically be extended to the full scope of the statute, because to do otherwise would be to give effect to the disjunctive phrasing of § 2(b) for the first time. *See* FCC Br. 34; *id.* at 21. Merely to state that position is to refute it.

Third, replaying an argument already rejected by this Court in *Louisiana*, the FCC appeals to a form of pseudo-legislative history to narrow § 2(b). The FCC claims that § 2(b) was passed in response to the intrastate authority that the Interstate Commerce Commission had been permitted to exercise in the *Shreveport Rate Case, Houston, E. & W.T.R. Co. v. United States*, 234 U.S. 342 (1914). That case involved ICC regulation of intrastate matters to which federal law did not directly apply — what the FCC now calls "ancillary"

jurisdiction. As a result, the FCC claims, whatever the terms of § 2(b), the provision should be limited to overruling *Shreveport* on its facts and to prohibiting similar exercises of "ancillary" jurisdiction. *See, e.g.*, FCC Br. 34-35; MCI Br. 45-47.

Even apart from the flaws this approach has as an attempt to elevate ambiguous legislative history over the terms of the statute, the FCC's maneuver is hobbled by a more fundamental error: this Court has already rejected this same argument. In *Louisiana*, the FCC claimed that because *Shreveport* had involved power to set intrastate rates, § 2(b) should only limit the FCC's power over that precise subject. The Court emphatically rejected this "narrow reading." *Louisiana*, 476 U.S. at 371. The Court explained that the provision was not limited to responding to the facts of the *Shreveport* case, but rather dealt more broadly with "[t]he question of an appropriate division between federal and state regulatory power." *Id.* at 372. The Court thus concluded that the "breadth of the language" in the section should be given full effect. *Id.* at 373. The FCC's effort to use *Shreveport* to cabin the terms of § 2(b) is thus a tactic that has already been soundly rejected.

The FCC's *final* attempt to slip out from under § 2(b) is a belated assertion of the so-called "impossibility" exception. FCC Br. 36. As described by the Court of Appeals, "this quite narrow exception," recognized in some court of appeals decisions, "provides that the FCC may preempt state regulation of intrastate telecommunications matters only when (1) it is impossible to separate the interstate and intrastate components of the FCC regulation and (2) the state regulation would negate the FCC's lawful authority over interstate communications." Pet. App. 16a. The FCC claims that this exception grants it pricing authority because local telephone facilities carry *both* intrastate and interstate calls.

The agency's belated resort to this theory is fruitless for a number of reasons.

First, the FCC never relied on this basis for jurisdiction in the First Report and Order. J.A. 448-56, 461-65 (¶¶ 83-103, 111-20). (outlining the FCC's grounds for authority). It is a bedrock principle of administrative law that a reviewing court "must judge the propriety of [administrative] action solely by the grounds invoked by the agency," *SEC v. Chenery Corp.*, 332 U.S. 194, 196 (1947), including the agency's articulated rationale for bringing its action within its statutory authority, *see American Textile Mfrs. Inst., Inc. v. Donovan*, 452 U.S. 490, 539-540 (1981). The *post hoc* impossibility claims of the FCC's appellate counsel thus cannot be substituted for the agency's own basis for acting.

Indeed, the policies behind *Chenery* apply with particular force here. Had the agency ever attempted to spell out its impossibility analysis, it would have been patently obvious that the theory could not remotely apply to a large portion of the FCC's claims for power. For example, setting wholesale prices for local service by definition involves matters that are solely *intrastate* in nature. Indeed, before the Eighth Circuit the FCC conceded that this service was "solely intrastate." Brief for the FCC and the United States at 30. The impossibility exception thus cannot remotely justify the wholesale pricing authority the FCC claimed. The FCC, moreover, has never claimed that jurisdiction to set wholesale prices under § 252(d)(3) should rest with a different entity from authority to set prices for interconnection and network elements under § 252(d)(1). As a result, the incontestable failure of the FCC's "impossibility" theory as to wholesale pricing necessarily undermines the FCC's claims over the remaining pricing authority as well.

But even if the FCC could get beyond both *Chenery* and the patent inapplicability of the impossibility exception to much of the authority the FCC wants to claim, that exception would still not justify FCC power over *any* pricing matter. Impossibility analysis protects the efficacy of the FCC's rulemaking authority only where the FCC has clear authority

over some interstate matter to start with. But the FCC itself acknowledges that the Act assigns authority over pricing as one indivisible unit (covering, for example, element pricing whether the elements are used for *inter*state or *intra*state calls), *see* FCC Br. 36-37, and the best the FCC can plausibly argue to get its foot in the door is that the Act has not been entirely clear in *foreclosing* any FCC role. From that starting point the FCC cannot call on "impossibility" to bootstrap a purported *ambiguity* about pricing into *complete control* for itself over the very same subject — unless the exception is an entirely circular device for expanding FCC power. To the contrary, impossibility analysis requires a clear FCC role in some *inter*state matter as an essential predicate for extending the FCC's reach into *intra*state matters. It cannot convert a purported lack of clarity into an absolute assignment of all pricing authority to the FCC.

3. The Court of Appeals Was Also Correct That Section 2(b) Restricts the FCC's Jurisdiction Over Other, Non-Pricing Matters Involving Intrastate Telecommunications.

Having relied on § 2(b) to provide "belt-and-suspenders" support for its ruling on jurisdiction over pricing, the Eighth Circuit was entirely correct to apply the plain terms of § 2(b) to restrict the FCC's authority over other, non-pricing intrastate matters addressed by the 1996 Act as well. As the court explained, Congress used express and unambiguous terms to assign the FCC a role in several intrastate matters under the Act. Absent such an express grant of authority, the FCC could point to no basis for ignoring the command of § 2(b). As a result, the court correctly held that the FCC's intrastate authority under § 251 was "confined to the six areas where

Congress expressly called for the FCC's participation." Pet. App. 37a.[21]

II. THE EIGHTH CIRCUIT PROPERLY VACATED ONE OF THE FCC'S FOUR RULES RADICALLY EXPANDING THE UNBUNDLING DUTY, BUT FAILED TO ENFORCE THE REMAINING RESTRICTIONS IMPOSED BY CONGRESS.

As explained above, Congress balanced a series of competing concerns as it opened local markets to competition. While seeking to encourage immediate entry by granting access to incumbents' facilities, at the same time Congress sought to protect incentives for facilities-based competition, ensure that incumbents would be fully compensated for the use of their property, and preserve support for universal service. The FCC wholly upset the balance reconciling these objectives by driving a freight train through each of four critical limitations Congress placed on incumbents' duty to provide access to elements of the network.

First, it redefined "network element[s]" to include *all* significant aspects of an incumbent's business, not just pieces of its call delivery system (and the features thereof). *Second*, it effectively read out of the Act the standards requiring the agency to evaluate whether access to network elements was "necessary" or whether denial of access would "impair" the ability of competitors to provide service. *Third*, it transformed the Act's requirement that an incumbent sell its competitor individual *pieces* of its network into an obligation to sell the entire network. *Finally*, the FCC attempted to force incumbents to provide a package of "unbundled" network

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[21] By identifying these areas of FCC power under § 251, the court did not purport to catalogue *all* grants of intrastate authority to the FCC in the Act. The question whether the FCC could identify sufficiently explicit language elsewhere in the Act to grant intrastate authority is not presented here.

elements already combined together into completed telephone service with all advanced features and functions.

The Eighth Circuit rightly vacated the last of these four extra-statutory efforts to redefine the unbundling duty. Each of the first three expansions of the duty is also flatly contrary to the Act. In upholding those FCC rules on unbundling, the Eighth Circuit erred.

A. The Combined Effect of the FCC's Four Unlawful Decisions on Unbundling Highlights the Conflict Between the FCC's Rules and the Act.

As outlined in detail below, the FCC violated the plain terms of the Act with each of its four expansions of the unbundling duty. But the stark disparities that exist between the FCC's individual rules and the terms of the Act do not tell the whole story here. It is the cumulative effect of the FCC's decisions that graphically shows how the FCC has expanded access to unbundled elements beyond all confines and turned it into an irresistible opportunity for entrants to engage in arbitrage at the expense of universal service.

The Eighth Circuit properly recognized the need to evaluate the FCC's rules against the plan of the Act as a whole. Thus, in vacating the FCC's attempt to require incumbents to provide network elements already combined together, the court explained that, viewed in the context provided by the broader structure of the Act, the FCC's rule would improperly "obliterate the careful distinctions Congress has drawn" between network elements and resale. Pet. App. 71a.

Indeed, the court's ruling prevented the FCC's multiple expansions of the unbundling duty from completely undoing the Act. As outlined above, the FCC's authorization of "sham unbundling" — allowing an entrant to order finished service through the fiction of purchasing *all* the elements of the network already preassembled into a functioning platform — would have given entrants an irresistible choice. Either they

could purchase service for resale at a price that contributes to universal service and fully compensates the incumbent (*i.e.*, the wholesale price under § 252(d)(3)), or they could purchase it *for a fraction of that price* through a rate that evades any contribution to universal service and fails to compensate the incumbent.

That is some choice! It would allow new entrants to pay a fraction of the price of wholesale service through the expedient of invoking sham unbundling and ordering the network element "platform." Perhaps most outrageous of all, this government-sponsored system of regulatory arbitrage would have allowed entrants not merely to avoid contributing to universal service, but — while doing nothing but reselling service provided entirely over an incumbent's network — to pocket for themselves the revenues from business and urban customers that currently maintain low residential rates. In that way, sham unbundling would effectively convert what had been a subsidy for consumers into a subsidy attracting arbitrageurs.

Not surprisingly, the FCC and its allies recognize that a candid examination of the effects of these rules provides the greatest threat to sham unbundling. Thus, they hope to divert attention from the complete picture in two ways.

First, they decry any effort to examine the statutory structure as an extra-textual foray into "policy." *See, e.g.*, FCC Br. 47; MCI Br. 21-22. The FCC no doubt would prefer to restrict this Court to viewing in isolation each of the discrete terms the agency purported to interpret. In that way, the FCC could attempt to squeeze some ambiguity out of the text and rush to claim deference for its construction. *See* FCC Br. 48; MCI Br. 14-15.

But this "divide and conquer" approach to statutory interpretation is impermissible. The FCC cannot jump to *Chevron* to shore up its rules while hiding the overall impact of

its regulatory scheme. To the contrary, before there can be any question of deferring to an agency, a court must endeavor to determine the intent of Congress by examining both "the particular statutory language at issue *as well as the language and design of the statute as a whole*." *Sullivan v. Everhart*, 494 U.S. 83, 89 (1990) (emphasis added); *United States Sav. Ass'n v. Timbers of Inwood Forest Assocs., Ltd.*, 484 U.S. 365, 371 (1988). As the Court has warned, individual provisions are "often clarified by the remainder of the statutory scheme," in particular where "only one of the permissible meanings produces a substantive effect that is compatible with the rest of the law." *Timbers of Inwood*, 484 U.S. at 371. *Chevron* cannot be applied, so to speak, on an "unbundled basis."

Nor can the FCC bolster its attacks on the Eighth Circuit's construction of the Act with its vitriolic rhetoric. What the FCC and its supporters vilify as anticompetitive increases in costs that the Eighth Circuit imposed due to its "policy" views, *see, e.g.*, MCI Br. 22, AT&T Br. 46, involve nothing more than enforcing the balanced restraints Congress imposed on access to elements.

MCI attempts a second, more focused effort to impose blinders on any analysis of the Act by insisting that the impact of the FCC's sham unbundling on universal service must be ignored. Universal service, MCI claims, is an entirely separate concern addressed elsewhere in the Act. Thus, pointing to the mandate for new "explicit" subsidies, *see* § 254, MCI claims that Congress refused to link such reforms in any way to competitors' ability to enter the market. MCI would brand any effort to show that the FCC's rules would exempt entrants from the burdens of existing implicit subsidies as a misguided effort to "preserve" the subsidies Congress wanted replaced. MCI Br. 25. But MCI well knows that GTE and other incumbents have no desire to preserve implicit subsidies. Rather, they would prefer a rapid transfer to the explicit funding systems that will ensure that all carriers bear an equal burden. But what

Congress explicitly forbade is a system in which incumbents continue to bear *all* the burdens of paying for universal service while entrants are freed from *any* universal service obligations and can undercut incumbents' rates simply by reselling use of the incumbent's own network. That result patently conflicts with Congress's repeated efforts to preserve universal service funding — including the unequivocal command that "[e]very telecommunications carrier . . . *shall contribute, on an equitable and nondiscriminatory basis*" to universal service. § 254(f). *See also* § 253(b) (preserving States' authority to impose "competitively neutral" means for advancing universal service). Despite MCI's hopes, that unqualified command does not permit competitors to enter the market for *any period* without contributing to universal service.

MCI desperately claims that Congress required *no* coordination between introducing competition and spreading universal service burdens equitably to entrants for one reason — MCI cannot deny that sham unbundling will have precisely the effect of promoting arbitrage and freeing entrants from any obligation to contribute to universal service. MCI thus strains to reconcile the statutory plan with the windfall promised by the FCC by ignoring Congress's commands requiring *all* carriers to bear the load of universal service.

These attempts to divert attention from the cumulative effects of the FCC's actions should fail. As detailed below, the conflicts between each of the FCC's rules and the terms of the Act provide ample reason for vacating the agency's actions. But the overall impact of the FCC's rules on unraveling the plan crafted by Congress also provides an important part of the picture demonstrating that the agency's actions cannot be reconciled with the language and structure of the Act.

B. The Court of Appeals Erred in Upholding Three of the FCC's Improper Expansions of the Duty To Provide Unbundled Network Elements.

While it prevented the worst harm that would result from the FCC's expansions of the duty to unbundle by vacating the rule requiring incumbents to provide elements preassembled, the Court of Appeals erred in upholding three of the FCC's major decisions broadening the unbundling duty.

1. The FCC Improperly Expanded the Definition of Network Elements.

The FCC erred first and foremost by ignoring the express limits in the definition of "network elements" and expanding the term beyond all rational bounds. Congress restricted the term so that entrants could obtain parts of the incumbent's call-routing network. The plain and ordinary meaning of the term "network element" itself, after all, denotes a "piece" of the "network" — that is, the system of lines and switches that makes up the local exchange. The statutory definition confirms that commonsense understanding as it restricts a network element to a "facility or equipment," § 153(29) — that is, a physical piece of the network. While the definition also encompasses "features, functions, and capabilities" of these network parts, it includes only features or functions that are "provided *by means of such facility or equipment*." *Id.* (emphasis added). Congress thus established network elements as items that are unalterably rooted in discrete physical parts of the local exchange.

The Act also restricts "network elements" by requiring that an element be "used in the provision of a telecommunications service." *Id.* "Telecommunications," in turn, is defined as the "transmission, between or among points specified by the user, of information of the user's choosing." § 153(46). Network elements, therefore, are the pieces of "equipment" that make up the incumbent's "network" for call delivery — the system used

to transmit calls from one point to another. Not surprisingly, this definition effectively makes network elements correspond to the so-called "bottleneck" facilities of the local exchange that are necessary for any carrier to use to get calls to and from every customer in a local exchange area. It is precisely that type of capital-intensive infrastructure owned by the incumbent that entrants might find difficult to duplicate in the near term when first starting their own local telephone businesses.

Both the FCC and the Eighth Circuit, however, removed any constraints limiting what might count as a network element and converted the term into an avenue for entrants effectively to rent any part of an incumbent's business. Following the FCC, the court emphasized that elements were facilities used in providing "telecommunications *service*," and that telecommunications service is the "'offering of telecommunications . . . to the public.'" Pet. App. 42a (emphasis added) (quoting § 153(46)). In the court's view, "offering" service to the public encompassed many functions beyond routing calls, and thus "network elements" were not limited to parts of the actual call-routing network at all. *Id.*

But that expansive gloss cuts the term loose from any plausible connection to the text. Indeed, it removes any constraint at all on what can be a network element. Everything that a LEC does and everything that it uses in its business is, in some sense, part of the "overall commercial offering" of service to the public. Pet. App. 43a. By making anything used in the offering of service the only touchstone for deciding what is an element, the court endorsed an FCC construction that guarantees absurd results. Under the FCC's reading, an incumbent's entire billing department and all the software and "equipment" it uses would be an "element" subject to being rented out to entrants on an "unbundled basis."

The terms of the definition, moreover, make it plain that the reference to the "provision of telecommunications service" — the phrase on which the FCC so heavily relies — was not

designed to decouple "network elements" from the familiar and concrete concept of the call-routing network. The definition refers to facilities (including their features) "used in the transmission, routing, or other provision of a telecommunications service." § 153(29). That listing shows that, far from straining to sweep in every function performed by a LEC to operate a profitable business, Congress was referring to basic steps in call delivery. The specific functions Congress described — "transmission" and "routing" — both refer to physical delivery of calls. The concluding term in the list referring to "other provision" of service does not suddenly expand the sentence to encompass every aspect of running a local exchange business. To the contrary, under the principle of *ejusdem generis*, such a general term concluding a list is limited by the more specific terms that precede it. *See, e.g.*, *Breininger v. Sheet Metal Workers*, 493 U.S. 67, 91-92 (1989). The FCC's contrary reading is utterly at odds with the text.[22]

By automatically treating as "network elements" everything that a LEC uses in any aspect of its business, the FCC absolved itself of the responsibility of ever applying the terms actually set by Congress. Before requiring unbundling, the FCC never even considered whether a given item at issue was actually a "facility or equipment" that was a part of the network (or a "featur[e], functio[n], or capabilit[y]" of such a facility). This approach makes "network elements" infinitely expandable, and the Eighth Circuit applied this reading to uphold two FCC errors.

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[22] The FCC itself, moreover, has interpreted the same terms in another section of the Act to mean precisely what we suggest. Under § 214(e), a carrier's eligibility for a new federal support mechanism hinges, in part, upon whether the carrier is "using its own facilities" to "offer" certain telecommunications "services." § 214(e)(1)(A). The FCC has squarely ruled that under that section the term "facilities" is limited to "physical components of the telecommunications network that are used in the transmission or routing" of calls. Universal Service Order ¶ 151.

(a) The FCC Erred By Treating Discrete Services as Network Elements.

First, the FCC concluded not only that "network elements" could include any equipment used in any aspect of the LEC's business, but also that an entire branch of the business might be treated as an "element." The agency thus decided that operator and directory assistance services would be treated as network elements — producing the absurdity that live operators are deemed "elements" of the network subject to unbundling.[23] J.A. 125-29 (¶¶ 534-40). Such an outcome cannot be squared with the terms of the statute. Operators providing directory assistance or other service to customers cannot be forced into the statutory categories of a "facility" or "equipment" or even "features, functions, or capabilities provided by means of such facility or equipment." § 153(29). To the contrary, they are *people* fulfilling a role in running one aspect of the LEC's business.

Operators, moreover, are used to provide a distinct *service*, and the Act provides a separate means for entrants to obtain services from an incumbent under the resale provisions of § 251(c)(4). The Eighth Circuit's bald conclusion that § 251(c)(4) does not provide the "exclusive means" for entrants to obtain services for resale, Pet. App. 45a, but that services should *also* be available as "network elements," ignores both the text and legislative history. Where a statute addresses discrete, defined terms such as finished "services" and "network elements" in separate provisions, the inclusion of one term in a given provision necessarily implies exclusion of the

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[23] Indeed, as if to pursue its own *reductio ad absurdum*, the FCC suggested that, where technically feasible, when an entrant such as AT&T "leases" a GTE operator on an "unbundled basis," that operator should be "rebranded" — *i.e.*, the operator should selectively identify himself or herself as an AT&T operator when answering a call from an AT&T customer. J.A. 127-28 (¶ 537).

other. *See, e.g., O'Melveny & Myers v. FDIC*, 512 U.S. 79, 86 (1994) ("*Inclusio unius, exclusio alterius.*").

Here the evolution of the Act strongly confirms that reading since Congress consciously eliminated any reference to "services" in the definition of network elements. Both the House and Senate bills had referred to unbundled access to "services" — indeed, the Senate bill did not even contain a separate provision on resale of services. *See* S. 652, 104th Cong., 1st Sess. § 251(b)(1) (1995); H.R. 1555, 104th Cong., 1st Sess. § 242(a)(2) (1995). In the Act, however, any mention of services was eliminated from both the definition of network elements and the section outlining the unbundling duty, *see* § 251(c)(3). Instead, "services" were addressed solely in the separate resale provision, § 251(c)(4). The FCC's expansion of elements to include operator and directory assistance services is thus wholly at odds with the Act.

(b) The FCC Improperly Expanded the Definition of Elements To Include OSS.

Second, the FCC determined that background software systems used by an incumbent to run its business, known as operation support systems (OSS), would qualify as elements. OSS perform a number of functions. The vast majority are software systems designed to maximize the efficiency of the LEC's operations, and in particular its customer service operations. Thus, such software manages billing functions, automatically routes service requests entered by a customer service operator to the appropriate personnel, allows scheduling of repair visits, and provides access to customer information relevant to the process of ordering services or repairs.

None of these systems is part of the call-routing network. By limitlessly expanding the definition of network elements, however, the FCC eliminated any need even to *consider* whether a particular software system actually has anything to

do with the "network" itself. Instead, it treated all OSS as "elements" of the "network" subject to unbundling without any further inquiry.

But OSS are not "facilities" or "equipment" used in the routing or transmission of a telephone call. Nor are they "features, functions, [or] capabilities that are provided by means of such facility or equipment." § 153(29). The FCC, moreover, made no effort to claim that OSS played a part in routing a call. Rather, the agency asserted that access to OSS was necessary to ensure that entrants could accomplish "pre-ordering, ordering . . . and billing," J.A. 118 (¶ 518), as well as "service functions [such] as scheduling customer appointments," *id.* at 118-19 (¶ 519), in "substantially the same time and manner that an incumbent can for itself," *id.* at 118 (¶ 518). The agency thus sought to ensure, through access to software, that entrants would be able to run the business aspects of their ventures just as efficiently as incumbents. The duty Congress imposed to provide "elements" of a telecommunications "network," however, had nothing to do with making such business skills of an incumbent available for its competitors.

(c) Expanding "Network Elements" to All Important Parts of a LEC's Business Defeats the Objectives of the Act.

The FCC's expansion of the definition of "network elements" is not only inconsistent with the terms of the Act, it is also wholly at odds with the statute's purposes. The Act is meant to promote competition by allowing new entrants to use the essential facilities of an incumbent — those aspects of the LEC's infrastructure that cannot reasonably be duplicated in the near term. But it does not foster competition to allow a competitor to purchase *all* significant parts of a LEC's business (especially at rates based on the costs of a hypothetical, most-efficient provider). Rather, true competition is promoted (and the benefits of innovation and improved efficiency are obtained) when an entrant has an incentive to provide some

aspects of a local exchange business more efficiently than the incumbent.

The FCC, however, requires a LEC to turn over to its competitors precisely those aspects of its business in which competitors should be attempting to differentiate themselves. In a competitive marketplace where a basic set of essential facilities was provided to all comers by the incumbent, competition would occur precisely on such non-essential aspects of the business as operator services, directory assistance, and operation support systems. By treating such parts of the business as "essential facilities," the FCC ensures that there will be no competition on these aspects of the business and limits competition merely to marketing functions.

2. The FCC Improperly Diluted the Standards Limiting What Elements Must Be Unbundled.

The FCC compounded its errors by eviscerating the standards in § 251(d)(2) limiting the obligation to unbundle even items that come within the definition of "network elements." Congress insisted that there be an evaluation of *need* before entrants would be granted forced access to the facilities of an incumbent's existing network. Thus, Congress directed that "in determining what network elements should be made available," the FCC "*shall consider*, at a minimum," whether access to proprietary elements was "necessary" and whether the failure to provide access to a non-proprietary element would "impair" an entrant's ability to provide service. § 251(d)(2) (emphasis added).

The FCC followed a two-step approach to read those limitations out of the Act. To start, the agency misinterpreted § 251(c)(3)'s direction concerning *where* an incumbent had to provide access to elements ("at any technically feasible point") as a command defining *what* had to be unbundled. The agency thus created an extra-statutory presumption that any element

that could technically be unbundled must be unbundled. J.A. 49 (¶ 278). The Eighth Circuit rightly vacated that presumption as contrary to the text, Pet. App. 46a-47a, and the FCC has not even attempted to seek review of that ruling. The Eighth Circuit failed to appreciate, however, that the agency's erroneous presumption fundamentally clouded the rest of the FCC's approach to the statutory terms limiting unbundling.

Specifically, when the FCC turned to § 251(d)(2), it perceived a false tension between the restrictions in that section and the blanket presumption it had mistakenly created under § 251(c)(3). To resolve that tension, the FCC gave primacy to its misconstruction of § 251(c)(3) and sought to read § 251(d)(2) in a way that would not "significantly diminish the obligation imposed by section 251(c)(3)." J.A. 53-54 (¶ 286). As a result, the FCC watered down the standards of § 251(d)(2) into meaninglessness by concluding that any assessment of the "necessary" and "impair" standards should proceed solely by looking to the availability of alternative facilities *from within the incumbent's own network*. J.A. 51-52, 54-55 (¶¶ 283, 287). Thus, irrespective of cost or other considerations, the FCC rejected the suggestion that access to a proprietary element should not be considered "necessary" if a requesting carrier "can obtain the requested proprietary element from a source other than the incumbent." *Id.* at 51-52 (¶ 283). That approach to the text is insupportable. It defies the ordinary English meaning of the terms to pretend that an element from an incumbent's network is "necessary" (or that failure to provide it would "impair" one's ability to provide service) if it is readily available "from a source other than the incumbent."

In upholding this approach, the Eighth Circuit simply echoed the FCC's claim that if incumbents could "evade their unbundling duties whenever a network element could be obtained elsewhere," the use of elements for entry would be crippled because almost every element "could *theoretically* be duplicated *eventually*." Pet. App. 48a (emphasis added). But

that begs the question in two respects. First, the FCC did not preclude consideration only of *theoretical* facilities that did not exist and were not readily available. Rather, it categorically precluded all consideration of alternatives — even those that exist and are readily available (including deployed facilities such as the fiber optic cables used by cable television providers or the switches deployed by competitive access providers).

Second, the suggestion that looking to facilities outside the network would allow incumbents to "evade their unbundling duties" just assumes the answer to the question. Section 251(d)(2) *limits* the duty by restricting when elements must be provided. To suggest that incumbents "evade" their "dut[y]" if access is not required where there are readily available alternatives assumes that the obligation is to provide completely unfettered access to all parts of the network at all times. That is simply not the duty Congress established.

The FCC also sought to justify its approach by declaring that considering alternative facilities outside the network might require entrants to "duplicate unnecessarily" a part of the network. J.A. 51-52 ¶ 283). That purported rationale brazenly rejects the policies Congress sought to promote. "Unnecessary" "duplication" is simply the FCC's denigrating term for deploying competing facilities. But Congress required an evaluation of need before elements would be provided precisely to encourage the use of non-incumbent facilities and thereby to preserve the incentives for innovation and increased efficiency that come with facilities-based competition. The FCC derided that goal and proceeded to grant exactly the unlimited access Congress had forbidden.

3. The FCC Improperly Ruled that Entrants Could Provide Service Using *Solely* Network Elements.

The FCC continued its drive to expand the unbundling duty by determining that entrants could rely *solely* on network

elements to provide local service. In other words, without supplying any facilities of its own, an entrant could order the entire network from end to end as supposedly discrete, "unbundled" elements and rely on those facilities to offer service. J.A. 63-65 (¶¶ 338-41).

Section 251(c)(3) rules out the FCC's approach. The section requires incumbents to provide "access" to "elements" of the network at any "technically feasible point." It is directed at ensuring physical access to discrete pieces of the network at various points of possible connection so that entrants can use limited portions of the network — not at simply allowing an entrant to order the whole network, lock, stock and barrel. Turning that requirement for incumbents to split up the network and provide different pieces at various points into an obligation to provide everything an entrant might need to provide service, from start to finish, rewrites the Act.

The FCC's approach would also undermine the basic distinction Congress crafted between resale and network elements as modes of entry. In § 251(c)(4), Congress created a distinct method of entry that would allow competitors with no facilities to rely solely on the incumbent's network and to resell the incumbent's own service. Network elements, in contrast, provided a means for those with some facilities of their own to enter immediately by filling gaps in their networks with leased equipment. It reflected Congress's understanding that "*[s]ome* facilities and capabilities (*e.g.*, central office switching) will likely need to be obtained from the incumbent . . . as network elements." Conf. Rep. at 148. By instead converting network elements into a second route for obtaining from the incumbent everything needed to run a local exchange (including, under the FCC's erroneous definition, such added services as operators and directory assistance), the FCC undermined a critical protection built into the structure of the Act to promote the development of competing facilities.

The resale route Congress established was also carefully restricted to ensure that the quick and easy way to enter the market by completely piggy-backing on the incumbent would not lead to regulatory distortions. The FCC's conversion of access to selected network elements into a route for effectively renting everything needed to run a local exchange business improperly allows entrants to circumvent those protections.

For example, Congress set the wholesale pricing rule to ensure that entrants acting as middlemen will incorporate the *same* subsidy structure in their rates that an incumbent faces in its retail rates. Section 252(d)(3) thus requires wholesale rates "based on the retail rate" — a standard that "reflect[s] whether, and to what extent, the local dialtone service is subsidized by other services." H.R. Rep. No. 104-204, at 72 (1995). The FCC's conversion of access to parts into an obligation to provide the *entire* network, however, largely destroys that fundamental protection. The FCC would make it possible to rely solely on elements to provide service, thus converting network elements effectively into a second avenue for using the incumbent's network to resell the incumbent's service, but at a price different from the wholesale price.

Similarly, the FCC would allow entrants to circumvent restrictions Congress imposed on the use of resold service. Congress sought to ensure that large long distance companies would not be given an immediate advantage in seizing market share by being able to market their own long distance service jointly with local service resold from a Bell company — at least not until the Bell company would be able to compete effectively by providing long distance service in its own region. *See* 47 U.S.C. § 271(e)(1). That restriction was expressly designed "to provide parity between the Bell operating companies and other telecommunications carriers in their ability to offer 'one stop shopping' for telecommunications services." S. Rep. No. 104-23, at 43 (1995). The FCC, however, would allow entrants to evade that

limitation completely by relying solely on network elements effectively to resell an incumbent's service. J.A. 61-62 (¶ 335).

C. The Eighth Circuit Rightly Vacated the FCC's Rule Requiring Incumbents to Provide Elements Already Assembled into Platforms.

Finally, as if to guarantee that its rules would provide an absolute end-run around the protections Congress built into the Act's resale provisions, the FCC capped off its multi-step expansion of the unbundling duty by ruling that incumbents would be required to provide elements *already preassembled* into functioning platforms whenever the elements were already connected in the incumbent's own network. *See* 47 C.F.R. § 51.315(b). That rule completed the FCC's conversion of unbundled elements into a second route for obtaining finished service to resell, since it guarantees that an entrant would not have to do anything for itself to turn disparate elements into a fully functioning service. By allowing entrants to engage in the fiction of labeling a request for use of the entire network as a request for "access" to "unbundled" elements, the FCC created a new, wholly extra-statutory duty and turned ordering "unbundled" elements into a sham. By imposing a duty to provide discrete, separate *parts* of the network, Congress did not require incumbents to turn over a *fully preassembled*, functioning network. The FCC's approach is akin to turning a requirement that a company provide entrants spare auto parts "on an unbundled basis" into a duty instead to provide entire automobiles ready to drive off the lot.

Creating that sweeping obligation is flatly contrary to the Act in its own right, but it is an even more egregious violation when combined with the pricing standard applied to network elements. As explained above, the pricing terms for network elements have been construed by regulators to exclude any consideration of the costs of universal service. By labeling its request to use the entire network as a fictional purchase of fully pre-assembled "elements," an entrant can effectively obtain the

same ability to resell an incumbent's service that it would get under the Act's resale provisions, but at a price that eliminates any contribution to universal service. The entrant thereby receives an automatic ability to undercut an incumbent's retail rates. The entrant would be assured of a chance to strip away the customers that currently support universal service and simultaneously to pocket for itself the funds those customers provided to subsidize low rates for the average consumer. The FCC's scheme would thus scuttle all the protections Congress built into the Act to ensure that allowing entrants a chance to piggy-back on an incumbent's network would *not* undermine the goal of universal service.

As the Eighth Circuit rightly held, the FCC's rule disregards the terms of § 251(c)(3). To start, that section expressly requires incumbents to provide "access to network elements" at "any technically feasible point" within the network. With those terms, Congress plainly cast the duty it imposed in terms of physical "access" to *pieces* of the network at different physical locations where connection might be feasible. The language plainly denotes a duty to provide access to multiple different parts of the network, not an obligation to turn over the entire network as one integrated, functioning unit. The section goes on, moreover, to specify that elements are to be provided on an "unbundled basis," again reinforcing the conclusion that Congress was requiring incumbents to provide *parts* of their network separated out for individual purchase.

Finally, as the Eighth Circuit emphasized, the section concludes by specifying that incumbents are required to provide elements only "'in a manner that allows *requesting carriers to combine* such elements in order to provide such telecommunications service." Pet. App. 70a (quoting 47 U.S.C. § 251(c)(3) (emphasis added by court)). As the court explained, "[t]his sentence unambiguously indicates that requesting carriers will combine the unbundled elements themselves." *Id.* That in itself makes it crystal clear that

Congress did not require incumbents to shoulder the burden of "combining" elements. Moreover, the section makes clear that entrants will have to go through this process of "combin[ing]" elements "in order to provide" service. "Elements" are thus the building blocks that must be put together to create a service that can be marketed to customers — elements in themselves do not come ready-made as services ready for entrants to turn around and resell.

The FCC tries in vain to avoid the plain terms chosen by Congress to define the unbundling duty. First, to divert attention from the language emphasized by the court below — which states that "requesting carriers" will "combine" network elements — the FCC casts its attack as if the judgment rested solely on the meaning of the term "unbundled." *See* FCC Br. at 44; *see also* MCI Br. 18-19. The FCC and its supporters thus claim that providing "elements" on an "unbundled basis" means only providing separate *prices* for elements and cannot imply that elements are actually to be sold on a physically separated basis.

That approach, however, ignores the context provided by the rest of the section. Section 251(c)(3) describes providing physical "access" to discrete "elements" of the network and dividing up the network into distinct parts where it will be "technically feasible" to connect to each separate element. In that context, providing this physical access "on an unbundled basis" necessarily requires separating out the parts of the network into distinct pieces.

Indeed, the FCC's approach to the phrase "on an unbundled basis" is incoherent. The FCC and its allies claim that "unbundling" goods means providing separate prices. But even in the antitrust and related contexts that they emphasize, requiring unbundling of goods does not imply simply the empty formality of creating a price list. To the contrary, it means requiring a firm to provide goods on a separated basis. Thus, even accepting the FCC's frame of reference, by

requiring "unbundling" the Act merely mandates that an incumbent cannot force a new entrant to purchase the entire network bundled together into completed telephone service. Rather, the LEC must also sell *pieces* of its network separately, at separate prices. But granting entrants the right to buy *pieces* of the network *not bundled* together is not the same as granting them the right to buy all the pieces of the network *already bundled together* into completed service.

In the end, even the FCC cannot avoid the plain import of the words of the Act. It explains in its brief, for example, that the point of the unbundling is to allow entrants "to lease *individual network elements*," FCC Br. 5 (emphasis added) — in other words, not the *whole network* already preassembled. Similarly, in its orders the FCC has repeatedly referred to "unbundling" an element to describe "physically separating" it from the rest of the network.[24] Given the context in which the term is used, in fact, it would be virtually impossible to discuss implementation of § 251(c)(3) without giving the term that connotation.

The FCC and its allies also place tremendous weight on dictionary definitions that appear to support the FCC's emphasis on separate prices. But as noted above, attempting to limit "unbundling" to imply solely a pricing constraint is illogical. In any event, AT&T and MCI wholly overplay their hand in claiming that merely citing dictionaries that appear to support the FCC's interpretation "is itself conclusive of its reasonableness." AT&T Br. 39; MCI Br. 19. Even the case cited by AT&T makes clear that the existence of a dictionary definition does not insulate an agency rule from review; rather,

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[24] *See, e.g.*, Third Order on Reconsideration, In the Matter of Implementation of the Local Competition Provisions in the Telecommunications Act of 1996, FCC 97-295, at 8 (Aug. 18, 1997) (stating that "transport is physically severable from switching" but that LECs "may not unbundle switching and transport facilities that are already combined").

the agency must still apply a definition that "mak[es] some sense under the statute." *National R.R. Passenger Corp. v. Boston & Me. Corp.*, 503 U.S. 407, 418 (1992). The Court, in fact, has rejected the view that "the courts must defer to the agency's choice among available dictionary definitions." *MCI v. AT&T*, 512 U.S. 218, 226 (1994). To the contrary, a choice among alternative dictionary definitions must be supported by "contextual indications" from the statute. *Id.* Here, the FCC's reading conflicts with the context of the Act. And in any event, even a dictionary cited by petitioners makes it plain that the term "unbundled" describes goods sold on a separate basis. *See* Random House Dictionary of the English Language 2055 (2d ed. 1987) ("(of related products or services) sold separately rather than as a package").

Nor can the FCC support its interpretation with its assertion that one network element — the signaling system — cannot be physically disconnected and provided separately to entrants. FCC Br. 45. The FCC's own Order undermines this claim. The FCC addressed explicitly the task of providing access to signaling, separate from the rest of the network, and ruled that "[c]arriers that provide their own switching facilities should be able to access the incumbent LEC's [signaling] network via a signaling link between their switch and the incumbent LEC's [signaling transfer point]" — a particular facility in the signaling network. J.A. 99-100 (¶ 483). Indeed, the FCC elaborated that "[t]his could be accomplished by the incumbent providing an unbundled signaling link from its [signaling transfer point] to the competitor's switch." Moreover, to the extent that the switching function cannot be separated from signaling associated with it, the FCC defined signaling to be part of the "switching" network element -- not a separate element at all. See 47 C.F.R. § 51.319(c)(1)(C)(2).

The FCC's purportedly "textual" arguments ring particularly hollow, moreover, since the FCC has not even attempted to resuscitate its vacated rules requiring incumbents

to combine elements in *new* ways upon an entrant's request. *See* 47 C.F.R. § 51.315(c)-(f). After conceding that § 251(c)(3) means that incumbents cannot be forced to do *additional* combining of elements, the FCC cannot point to any basis for requiring incumbents to provide *existing* combinations. The distinction between what *has been* combined and what *might be* combined brings the FCC's rule no closer to the text of the Act. The Act does not require incumbents to do combining for entrants, and the fact that an incumbent may have already added value to one set of elements by combining them for itself does not mean that entrants automatically get to free-ride on the incumbent's efforts. To the contrary, § 251(c)(3) sets a duty to turn over discrete pieces of the network, without the added benefit of combinations, and that is all it requires. The facile protest that incumbents will be "taking apart" their networks to provide those pieces cannot change the contours of that duty.

Next, the FCC and its supporters claim that in requiring incumbents to provide elements "in a manner that allows requesting carriers to combine" them, the Act imposes a "duty," and that "as a matter of grammar," a "duty" cannot be read to create a "right" for incumbents to insist on providing elements on a physically separated basis. FCC Br. 45. But this is nothing more than a semantic game. The terms of § 251(c)(3) necessarily *limit* the extent of the duty imposed by the Act. Because Congress has directed that incumbents are required to provide elements "in a manner that allows requesting carriers to combine" them, the necessary result is that incumbents remain free to insist that they will not provide elements in any other manner.

Lastly, the FCC appeals to § 251(c)(3)'s command for "nondiscriminatory access" to elements. FCC Br. 46. In the FCC's view, an entrant will have equal access to *all* an incumbent's elements only if it has the exact same ability as an incumbent to use the elements already connected together into

a functioning network. But using the nondiscrimination principle to unravel all the other limitations in the section would plainly prove too much. It is simply not discriminatory for an incumbent to fulfill its duty to provide elements "in a manner that allows the requesting carrier to combine" them by actually providing separate elements that entrants can combine — even if it means separating the individual elements. To use the analogy from above, a firm with a duty to provide spare auto parts does not "discriminate" against entrants by providing perfectly good parts instead of fully assembled cars.

Finally, the FCC and its allies again appeal to purported policy concerns as they complain that, in their view, the elimination of the network element "platform" has destroyed the utility of elements as a means of entry. That is nonsense. Nothing in the Eighth Circuit's decision undermines the efficiency of network elements as a means of entry. The Eighth Circuit merely put an end to the fiction of a pre-combined network element platform that would allow entrants to buy completed services for two to three times the discount required under the statutory pricing standard. Despite their complaints, there can be no serious doubt about what has slowed the advance of competition since the passage of the Act. As long as the option of sham unbundling was dangled before entrants, no rational firm would dare attempt either deploying its own facilities or reselling service under the Act's wholesale provisions. In short, the FCC's own implausible and yet irresistible offer of windfall profits through sham unbundling brought any plans for genuine entry — either facilities-based or through resale — effectively to a halt.

III. THE EIGHTH CIRCUIT PROPERLY VACATED THE "PICK-AND-CHOOSE" RULE AS AN UNREASONABLE CONSTRUCTION OF THE ACT.

Section 252(i) sets forth an unremarkable nondiscrimination principle designed to allow later entrants to obtain in negotiations the same terms for their agreements as carriers

who have gone before them, as long as they are willing to accept *all* the terms that formed the earlier bargain. The Act provides only that an incumbent "shall make available any interconnection, service, or network element provided under an agreement" to "any other requesting telecommunications carrier *upon the same terms and conditions as those provided in the agreement.*" § 252(i) (emphasis added).

In framing the issue under this section, the FCC conveniently omits the terms limiting incumbents' duty to providing "the same terms and conditions" as in an earlier agreement. *See* FCC Br. (I). That is hardly surprising, since the FCC's rules read that limitation out of the statute.

In the FCC's view, § 252(i) entitled a carrier "to choose among individual provisions" in an earlier agreement, J.A. 1044-45 (¶ 1310), and obtain those terms without even entering the standard negotiation process under § 252(a). *Id.* at 1048 (¶ 1321). Indeed, the FCC ruled that a carrier with a supposedly "binding" agreement in place could selectively jettison individual terms in favor of more advantageous terms subsequently negotiated by others. *Id.* at 1046-47 (¶ 1316). The FCC also ensured that a carrier could "choose" the terms it desired without having to accept corresponding tradeoffs elsewhere in the agreement that may have made those terms possible. Rather, to limit itself to providing the "same terms and conditions" as in an earlier agreement, an incumbent would have to "prove" that the terms were "*legitimately related* to the purchase of the individual element being sought." *Id.* at 1046 (¶ 1315). The FCC flatly determined that an incumbent "*may not*" treat terms governing sale of one element or service as part of the terms that produced agreement on another element or service. *Id.* (emphasis added). The FCC thus categorically rejected the possibility that concessions on their face related to

one particular piece of an agreement could have been a crucial *quid pro quo* for better terms on another.[25]

By artificially compartmentalizing every issue, the FCC's rule ignores the reality of bargaining and would make the give-and-take of negotiations impossible. An incumbent could never make a concession on one issue in return for a concession on another matter, because its own concession would automatically become available to all carriers without the need for others to accept the trade-off that made the term possible.

The Eighth Circuit rightly recognized this inherent conflict between the FCC's approach and Congress's design for implementing the Act. Despite the clear tension between the FCC's rule and the Act's unqualified requirement that incumbents need only offer "the same terms and conditions," the Eighth Circuit concluded that "the language of subsection 252(i) *in isolation*," did not prohibit the FCC's approach. Pet. App. 25a (emphasis added). Pursuing standard *Chevron* analysis, therefore, the court proceeded to "'look to the structure and language of the statute as a whole' to determine if the FCC's interpretation of this ambiguous provision is a reasonable one." *Id.* (quoting *National R.R. Passenger Corp. v. Boston & Maine Corp.*, 503 U.S. 407, 417 (1992)).[26] Despite the FCC's effort to label this approach pejoratively as a resort

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[25] The FCC's claim that it "protect[ed]" incumbents by requiring entrants using § 252(i) to adopt to the existing terms and conditions "*relating to the particular service or element*," FCC Br. 48 n.15 (emphasis added), is thus carefully worded to disguise the gaping hole in the supposed "protection" offered by the FCC's rule.

[26] While the court cast its analysis under the second step of *Chevron*, it would also have properly fit under the first. Examination of the structure and purposes of a statute is one of the "traditional tools of statutory construction," *Regions Hospital v. Shalala*, 118 S. Ct. 909, 915 (1998), to be employed before a statute is deemed ambiguous. *See also supra* p. 52.

to "policy," FCC Br. 49, consideration of the structure of the Act was a routine part of the process for determining whether an agency's action is "reasonable in light of the legislature's revealed design." *Nationsbank v. Variable Annuity Life Ins. Co.*, 513 U.S. 251, 257 (1995).

As the court explained, the "structure of the Act reveals Congress's preference for voluntarily negotiated interconnection agreements," Pet. App. 25a, and the FCC's rule would "thwart" that process, *id.* 26a. It would also conflict with the requirement that negotiated agreements be "binding," § 252(a)(1), because entrants could "unilaterally incorporate more advantageous provisions contained in subsequent agreements negotiated by other carriers." Pet. App. 26a. The Eighth Circuit thus correctly ruled that the FCC's approach to § 252(i) could not be reconciled with the Act.

As this Court has explained, "we should not impute to Congress a purpose to paralyze with one hand what it sought to promote with the other." *American Textile Mfrs. Inst., Inc. v. Donovan*, 452 U.S. 490, 513 (1981) (citations omitted). The FCC's rule would have achieved precisely that illogical result by undermining the process that Congress made the centerpiece for implementing the local competition terms of the Act.

CONCLUSION

For the foregoing reasons, the Court should resolve this case as follows:

First, the Court should affirm the Court of Appeals' judgments concerning both (i) the FCC's lack of authority over the pricing terms of the Act and (ii) the FCC's lack of authority over non-pricing intrastate matters covered by the Act.

Second, the Court should reverse the Court of Appeals' judgments upholding the FCC's rules (i) expanding the definition of network elements to include OSS and services such as directory assistance and operator services; (ii) diluting the "necessary" and "impair" standards of § 251(d)(2); and

(iii) declaring that entrants could rely solely on network elements to provide service.

Third, the Court should affirm the Court of Appeals' judgment vacating the FCC's rule requiring incumbents to provide network elements pre-assembled into combinations.

Fourth, the Court should affirm the Court of Appeals' judgment vacating the FCC's pick-and-choose rule.

Respectfully submitted,

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May 18, 1998

STATUTORY ADDENDUM

CONTENTS

47 U.S.C. § 152 APPLICATION OF ACT

* * *

(b) Except as provided in sections 223 through 227, inclusive, and section 332, and subject to the provisions of section 301 and title VI, nothing in this Act shall be construed to apply or to give the Commission jurisdiction with respect to (1) charges, classifications, practices, services, facilities, or regulations for or in connection with intrastate communication service by wire or radio of any carrier . . . .

* * *

47 U.S.C. § 153 DEFINITIONS

* * *

(29) NETWORK ELEMENT.- The term "network element" means a facility or equipment used in the provision of a telecommunications service. Such term also includes features, functions, and capabilities that are provided by means of such facility or equipment, including subscriber numbers, databases, signaling systems, and information sufficient for billing and collection or used in the transmission, routing, or other provision of a telecommunications service.

* * *

(43) TELECOMMUNICATIONS.- The term "telecommunications" means the transmission, between or among points specified by the user, of information of the user's choosing, without change in the form or content of the information as sent and received.

* * *

(46) TELECOMMUNICATIONS SERVICE.- The term "telecommunications service" means the offering of telecommunications for a fee directly to the public, or to such classes of users as to be effectively available directly to the public, regardless of the facilities used.

* * *

47 U.S.C. § 251 INTERCONNECTION.

(a) GENERAL DUTY OF TELECOMMUNICATIONS CARRIERS. - Each telecommunications carrier has the duty -

(1) to interconnect directly or indirectly with the facilities and equipment of other telecommunications carriers; and

(2) not to install network features, functions, or capabilities that do not comply with the guidelines and standards established pursuant to section 255 or 256.

(b) OBLIGATIONS OF ALL LOCAL EXCHANGE CARRIERS. - Each local exchange carrier has the following duties:

(1) RESALE. - The duty not to prohibit, and not to impose unreasonable or discriminatory conditions or limitations on, the resale of its telecommunications services.

(2) NUMBER PORTABILITY. - The duty to provide, to the extent technically feasible, number portability in accordance with requirements prescribed by the Commission.

(3) DIALING PARITY. - The duty to provide dialing parity to competing providers of telephone exchange service and telephone toll service, and the duty to permit all such providers to have nondiscriminatory access to telephone numbers, operator services, directory assistance, and directory listing, with no unreasonable dialing delays.

(4) ACCESS TO RIGHTS-OF-WAY. - The duty to afford access to the poles, ducts, conduits, and rights-of-way of such carrier to competing providers of telecommunications services on rates, terms, and conditions that are consistent with section 224.

(5) RECIPROCAL COMPENSATION. - The duty to establish reciprocal compensation arrangements for the transport and termination of telecommunications.

(c) ADDITIONAL OBLIGATIONS OF INCUMBENT LOCAL EXCHANGE CARRIERS. - In addition to the duties contained in subsection (b), each incumbent local exchange carrier has the following duties:

(1) DUTY TO NEGOTIATE. - The duty to negotiate in good faith in accordance with section 252 the particular terms and conditions of agreements to fulfill the duties described in paragraphs (1) through (5) of subsection (b) and this subsection. The requesting telecommunications carrier also has the duty to negotiate in good faith the terms and conditions of such agreements.

(2) INTERCONNECTION. - The duty to provide, for the facilities and equipment of any requesting telecommunications carrier, interconnection with the local exchange carrier's network-

(A) for the transmission and routing of telephone exchange service and exchange access;

(B) at any technically feasible point within the carrier's network;

(C) that is at least equal in quality to that provided by the local exchange carrier to itself or to any subsidiary, affiliate, or any other party to which the carrier provides interconnection; and

(D) on rates, terms, and conditions that are just, reasonable, and nondiscriminatory, in accordance with the terms and conditions of the agreement and the requirements of this section and section 252.

(3) UNBUNDLED ACCESS. - The duty to provide, to any requesting telecommunications carrier for the

provision of a telecommunications service, nondiscriminatory access to network elements on an unbundled basis at any technically feasible point on rates, terms, and conditions that are just, reasonable, and nondiscriminatory in accordance with the terms and conditions of the agreement and the requirements of this section and section 252. An incumbent local exchange carrier shall provide such unbundled network elements in a manner that allows requesting carriers to combine such elements in order to provide such telecommunications service.

(4) RESALE. - The duty -

(A) to offer for resale at wholesale rates any telecommunications service that the carrier provides at retail to subscribers who are not telecommunications carriers; and

(B) not to prohibit, and not to impose unreasonable or discriminatory conditions or limitations on, the resale of such telecommunications service, except that a State commission may, consistent with regulations prescribed by the Commission under this section, prohibit a reseller that obtains at wholesale rates a telecommunications service that is available at retail only to a category of subscribers from offering such service to a different category of subscribers.

(5) NOTICE OF CHANGES. - The duty to provide reasonable public notice of changes in the information necessary for the transmission and routing of services using that local exchange carrier's facilities or networks, as well as of any other changes that would affect the interoperability of those facilities and networks.

(6) COLLOCATION. - The duty to provide, on rates, terms, and conditions that are just, reasonable,

and nondiscriminatory, for physical collocation of equipment necessary for interconnection or access to unbundled network elements at the premises of the local exchange carrier, except that the carrier may provide for virtual collocation if the local exchange carrier demonstrates to the State commission that physical collocation is not practical for technical reasons or because of space limitations.

(d) IMPLEMENTATION. -

(1) IN GENERAL. - Within 6 months after the date of enactment of the Telecommunications Act of 1996, the Commission shall complete all actions necessary to establish regulations to implement the requirements of this section.

(2) ACCESS STANDARDS. - In determining what network elements should be made available for purposes of subsection (c)(3), the Commission shall consider, at a minimum, whether -

(A) access to such network elements as are proprietary in nature is necessary; and

(B) the failure to provide access to such network elements would impair the ability of the telecommunications carriers seeking access to provide the services that it seeks to offer.

(3) PRESERVATION OF STATE ACCESS REGULATIONS. - In prescribing and enforcing regulations to implement the requirements of this section, the Commission shall not preclude the enforcement of any regulation, order, or policy of a State commission that -

(A) establishes access and interconnection obligations of local exchange carriers;

(B) is consistent with the requirements of this section; and

(C) does not substantially prevent implementation of the requirements of this section and the purposes of this part.

(e) NUMBERING ADMINISTRATION. -

(1) COMMISSION AUTHORITY AND JURISDICTION. - The Commission shall create or designate one or more impartial entities to administer telecommunications numbering and to make such numbers available on an equitable basis. The Commission shall have exclusive jurisdiction over those portions of the North American Numbering Plan that pertain to the United States. Nothing in this paragraph shall preclude the Commission from delegating to State commissions or other entities all or any portion of such jurisdiction.

(2) COSTS. - The cost of establishing telecommunications numbering administration arrangements and number portability shall be borne by all telecommunications carriers on a competitively neutral basis as determined by the Commission.

(f) EXEMPTIONS, SUSPENSIONS, AND MODIFICATIONS. -

(1) EXEMPTION FOR CERTAIN RURAL TELEPHONE COMPANIES. -

(A) EXEMPTION. - Subsection (c) of this section shall not apply to a rural telephone company until (i) such company has received a bona fide request for interconnection, services, or network elements, and (ii) the State commission determines (under subparagraph (B)) that such request is not unduly economically burdensome, is technically feasible, and is consistent with section 254 (other than subsections (b)(7) and (c)(1)(D) thereof).

(B) STATE TERMINATION OF EXEMPTION AND IMPLEMENTATION SCHEDULE. - The party

making a bona fide request of a rural telephone company for interconnection, services, or network elements shall submit a notice of its request to the State commission. The State commission shall conduct an inquiry for the purpose of determining whether to terminate the exemption under subparagraph (A). Within 120 days after the State commission receives notice of the request, the State commission shall terminate the exemption if the request is not unduly economically burdensome, is technically feasible, and is consistent with section 254 (other than subsections (b)(7) and (c)(1)(D) thereof). Upon termination of the exemption, a State commission shall establish an implementation schedule for compliance with the request that is consistent in time and manner with Commission regulations.

(C) LIMITATION ON EXEMPTION. - The exemption provided by this paragraph shall not apply with respect to a request under subsection (c) from a cable operator providing video programming, and seeking to provide any telecommunications service, in the area in which the rural telephone company provides video programming. The limitation contained in this subparagraph shall not apply to a rural telephone company that is providing video programming on the date of enactment of the Telecommunications Act of 1996.

(2) SUSPENSIONS AND MODIFICATIONS FOR RURAL CARRIERS. - A local exchange carrier with fewer than 2 percent of the Nation's subscriber lines installed in the aggregate nationwide may petition a State commission for a suspension or modification of the application of a requirement or requirements of

subsection (b) or (c) to telephone exchange service facilities specified in such petition. The State commission shall grant such petition to the extent that, and for such duration as, the State commission determines that such suspension or modification -

(A) is necessary -

(i) to avoid a significant adverse economic impact on users of telecommunications services generally;

(ii) to avoid imposing a requirement that is unduly economically burdensome; or

(iii) to avoid imposing a requirement that is technically infeasible; and

(B) is consistent with the public interest, convenience, and necessity.

The State commission shall act upon any petition filed under this paragraph within 100 days after receiving such petition. Pending such action, the State commission may suspend enforcement of the requirement or requirements to which the petition applies with respect to the petitioning carrier or carriers.

(g) CONTINUED ENFORCEMENT OF EXCHANGE ACCESS AND INTERCONNECTION REQUIREMENTS. - On and after the date of enactment of the Telecommunications Act of 1996, each local exchange carrier, to the extent that it provides wireline services, shall provide exchange access information access, and exchange services for such access to interexchange carriers and information service providers in accordance with the same equal access and nondiscriminatory interconnection restrictions and obligations (including receipt of compensation) that apply to such carrier on the date immediately preceding the date of enactment of the Telecommunications Act of 1996 under any court order, consent decree, or regulation, order, or policy of the Commission, until such restrictions and

obligations are explicitly superseded by regulations prescribed by the Commission after such date of enactment. During the period beginning on such date of enactment and until such restrictions and obligations are so superseded, such restrictions and obligations shall be enforceable in the same manner as regulations of the Commission.

(h) DEFINITION OF INCUMBENT LOCAL EXCHANGE CARRIER. -

(1) DEFINITION. - For purposes of this section, the term "incumbent local exchange carrier" means, with respect to an area, the local exchange carrier that -

(A) on the date of enactment of the Telecommunications Act of 1996, provided telephone exchange service in such area; and

(B)(i) on such date of enactment, was deemed to be a member of the exchange carrier association pursuant to section 69.601(b) of the Commission's regulations (47 C.F.R. 69.601(b)); or

(ii) is a person or entity that, on or after such date of enactment, became a successor or assign of a member described in clause (i).

(2) TREATMENT OF COMPARABLE CARRIERS AS INCUMBENTS. - The Commission may, by rule, provide for treatment of a local exchange carrier (or class or category thereof) as an incumbent local exchange carrier for purposes of this section if -

(A) such carrier occupies a position in the market for telephone exchange service within an area that is comparable to the position occupied by a carrier described in paragraph (1);

(B) such carrier has substantially replaced an incumbent local exchange carrier described in paragraph (1); and

(C) such treatment is consistent with the public interest, convenience, and necessity and the purposes of this section.

(i) SAVINGS PROVISION. - Nothing in this section shall be construed to limit or otherwise affect the Commission's authority under section 201.

47 U.S.C. § 252 PROCEDURES FOR NEGOTIATION, ARBITRATION, AND APPROVAL OF AGREEMENTS.

(a) AGREEMENTS ARRIVED AT THROUGH NEGOTIATION. -

(1) VOLUNTARY NEGOTIATIONS. - Upon receiving a request for interconnection, services, or network elements pursuant to section 251, an incumbent local exchange carrier may negotiate and enter into a binding agreement with the requesting telecommunications carrier or carriers without regard to the standards set forth in subsections (b) and (c) of section 251. The agreement shall include a detailed schedule of itemized charges for interconnection and each service or network element included in the agreement. The agreement, including any interconnection agreement negotiated before the date of enactment of the Telecommunications Act of 1996, shall be submitted to the State commission under subsection (e) of this section.

(2) MEDIATION. - Any party negotiating an agreement under this section may, at any point in the negotiation, ask a State commission to participate in the negotiation and to mediate any differences arising in the course of the negotiation.

(b) AGREEMENTS ARRIVED AT THROUGH COMPULSORY ARBITRATION. -

(1) ARBITRATION. - During the period from the 135th to the 160th day (inclusive) after the date on

which an incumbent local exchange carrier receives a request for negotiation under this section, the carrier or any other party to the negotiation may petition a State commission to arbitrate any open issues.

(2) DUTY OF PETITIONER. -

(A) A party that petitions a State commission under paragraph (1) shall, at the same time as it submits the petition, provide the State commission all relevant documentation concerning -

(i) the unresolved issues;

(ii) the position of each of the parties with respect to those issues; and

(iii) any other issue discussed and resolved by the parties.

(B) A party petitioning a State commission under paragraph (1) shall provide a copy of the petition and any documentation to the other party or parties not later than the day on which the State commission receives the petition.

(3) OPPORTUNITY TO RESPOND. - A non-petitioning party to a negotiation under this section may respond to the other party's petition and provide such additional information as it wishes within 25 days after the State commission receives the petition.

(4) ACTION BY STATE COMMISSION. -

(A) The State commission shall limit its consideration of any petition under paragraph (1) (and any response thereto) to the issues set forth in the petition and in the response, if any, filed under paragraph (3).

(B) The State commission may require the petitioning party and the responding party to provide such information as may be necessary for the State commission to reach a decision on the unresolved issues. If any party

refuses or fails unreasonably to respond on a timely basis to any reasonable request from the State commission, then the State commission may proceed on the basis of the best information available to it from whatever source derived.

(C) The State commission shall resolve each issue set forth in the petition and the response, if any, by imposing appropriate conditions as required to implement subsection (c) upon the parties to the agreement, and shall conclude the resolution of any unresolved issues not later than 9 months after the date on which the local exchange carrier received the request under this section.

(5) REFUSAL TO NEGOTIATE. - The refusal of any other party to the negotiation to participate further in the negotiations, to cooperate with the State commission in carrying out its function as an arbitrator, or to continue to negotiate in good faith in the presence, or with the assistance, of the State commission shall be considered a failure to negotiate in good faith.

(c) STANDARDS FOR ARBITRATION. - In resolving by arbitration under subsection (b) any open issues and imposing conditions upon the parties to the agreement, a State commission shall -

(1) ensure that such resolution and conditions meet the requirements of section 251, including the regulations prescribed by the Commission pursuant to section 251;

(2) establish any rates for interconnection, services, or network elements according to subsection (d); and

(3) provide a schedule for implementation of the terms and conditions by the parties to the agreement.

(d) PRICING STANDARDS. -

(1) INTERCONNECTION AND NETWORK ELEMENT CHARGES. - Determinations by a State commission of the just and reasonable rate for the interconnection of facilities and equipment for purposes of subsection (c)(2) of section 251, and the just and reasonable rate for network elements for purposes of subsection (c)(3) of such section -

(A) shall be -

(i) based on the cost (determined without reference to a rate-of-return or other rate-based proceeding) of providing the interconnection or network element (whichever is applicable), and

(ii) nondiscriminatory, and

(B) may include a reasonable profit.

(2) CHARGES FOR TRANSPORT AND TERMINATION OF TRAFFIC. -

(A) IN GENERAL. - For the purposes of compliance by an incumbent local exchange carrier with section 251(b)(5), a State commission shall not consider the terms and conditions for reciprocal compensation to be just and reasonable unless -

(i) such terms and conditions provide for the mutual and reciprocal recovery by each carrier of costs associated with the transport and termination on each carrier's network facilities of calls that originate on the network facilities of the other carrier; and

(ii) such terms and conditions determine such costs on the basis of a reasonable approximation of the

additional costs of terminating such calls.

(B) RULES OF CONSTRUCTION. - This paragraph shall not be construed -

(i) to preclude arrangements that afford the mutual recovery of costs through the offsetting of reciprocal obligations, including arrangements that waive mutual recovery (such as bill-and-keep arrangements); or

(ii) to authorize the Commission or any State commission to engage in any rate regulation proceeding to establish with particularity the additional costs of transporting or terminating calls, or to require carriers to maintain records with respect to the additional costs of such calls.

(3) WHOLESALE PRICES FOR TELECOMMUNICATIONS SERVICES. - For the purposes of section 251(c)(4), a State commission shall determine wholesale rates on the basis of retail rates charged to subscribers for the telecommunications service requested, excluding the portion thereof attributable to any marketing, billing, collection, and other costs that will be avoided by the local exchange carrier.

(e) APPROVAL BY STATE COMMISSION. -

(1) APPROVAL REQUIRED. - Any interconnection agreement adopted by negotiation or arbitration shall be submitted for approval to the State commission. A State commission to which an agreement is submitted shall approve or reject the agreement, with written findings as to any deficiencies.

(2) GROUNDS FOR REJECTION. - The State commission may only reject -

(A) an agreement (or any portion thereof) adopted by negotiation under subsection (a) if it finds that -

(i) the agreement (or portion thereof) discriminates against a telecommunications carrier not a party to the agreement; or

(ii) the implementation of such agreement or portion is not consistent with the public interest, convenience, and necessity; or

(B) an agreement (or any portion thereof) adopted by arbitration under subsection (b) if it finds that the agreement does not meet the requirements of section 251, including the regulations prescribed by the Commission pursuant to section 251, or the standards set forth in subsection (d) of this section.

(3) PRESERVATION OF AUTHORITY. - Notwithstanding paragraph (2), but subject to section 253, nothing in this section shall prohibit a State commission from establishing or enforcing other requirements of State law in its review of an agreement, including requiring compliance with intrastate telecommunications service quality standards or requirements.

(4) SCHEDULE FOR DECISION. - If the State commission does not act to approve or reject the agreement within 90 days after submission by the parties of an agreement adopted by negotiation under subsection (a), or within 30 days after submission by the parties of an agreement adopted by arbitration under subsection (b), the agreement shall be deemed approved. No State court shall have jurisdiction to review the action of a State commission in approving or rejecting an agreement under this section.

(5) COMMISSION TO ACT IF STATE WILL NOT ACT. - If a State commission fails to act to carry out its responsibility under this section in any proceeding or other matter under this section, then the Commission shall issue an order preempting the State commission's jurisdiction of that proceeding or matter within 90 days after being notified (or taking notice) of such failure, and shall assume the responsibility of the State commission under this section with respect to the proceeding or matter and act for the State commission.

(6) REVIEW OF STATE COMMISSION ACTIONS. - In a case in which a State fails to act as described in paragraph (5), the proceeding by the Commission under such paragraph and any judicial review of the Commission's actions shall be the exclusive remedies for a State commission's failure to act. In any case in which a State commission makes a determination under this section, any party aggrieved by such determination may bring an action in an appropriate Federal district court to determine whether the agreement or statement meets the requirements of section 251 and this section.

(f) STATEMENTS OF GENERALLY AVAILABLE TERMS. -

(1) IN GENERAL. - A Bell operating company may prepare and file with a State commission a statement of the terms and conditions that such company generally offers within that State to comply with the requirements of section 251 and the regulations thereunder and the standards applicable under this section.

(2) STATE COMMISSION REVIEW. - A State commission may not approve such statement unless such statement complies with subsection (d) of this section and section 251 and the regulations thereunder. Except as provided in section 253, nothing in this section shall prohibit a State commission from establishing or enforcing other requirements of State

law in its review of such statement, including requiring compliance with intrastate telecommunications service quality standards or requirements.

(3) SCHEDULE FOR REVIEW. - The State commission to which a statement is submitted shall, not later than 60 days after the date of such submission -

(A) complete the review of such statement under paragraph (2) (including any reconsideration thereof), unless the submitting carrier agrees to an extension of the period for such review; or

(B) permit such statement to take effect.

(4) AUTHORITY TO CONTINUE REVIEW. - Paragraph (3) shall not preclude the State commission from continuing to review a statement that has been permitted to take effect under subparagraph (B) of such paragraph or from approving or disapproving such statement under paragraph (2).

(5) DUTY TO NEGOTIATE NOT AFFECTED. - The submission or approval of a statement under this subsection shall not relieve a Bell operating company of its duty to negotiate the terms and conditions of an agreement under section 251.

(g) CONSOLIDATION OF STATE PROCEEDINGS. - Where not inconsistent with the requirements of this Act, a State commission may, to the extent practical, consolidate proceedings under sections 214(e), 251(f), 253, and this section in order to reduce administrative burdens on telecommunications carriers, other parties to the proceedings, and the State commission in carrying out its responsibilities under this Act.

(h) FILING REQUIRED. - A State commission shall make a copy of each agreement approved under subsection (e) and each statement approved under subsection (f) available for public inspection and copying within 10 days after the agreement or statement is approved. The State commission

may charge a reasonable and nondiscriminatory fee to the parties to the agreement or the party filing the statement to cover the costs of approving and filing such agreement or statement.

(i) AVAILABILITY TO OTHER TELECOMMUNICATIONS CARRIERS. - A local exchange carrier shall make available any interconnection, service, or network element provided under an agreement approved under this section to which it is a party to any other requesting telecommunications carrier upon the same terms and conditions as those provided in the agreement.

(j) DEFINITION OF INCUMBENT LOCAL EXCHANGE CARRIER. - For purposes of this section, the term "incumbent local exchange carrier" has the meaning provided in section 251(h).

47 U.S.C. § 253 REMOVAL OF BARRIERS TO ENTRY.

(a) IN GENERAL. - No State or local statute or regulation, or other State or local legal requirement, may prohibit or have the effect of prohibiting the ability of any entity to provide any interstate or intrastate telecommunications service.

(b) STATE REGULATORY AUTHORITY. - Nothing in this section shall affect the ability of a State to impose, on a competitively neutral basis and consistent with section 254, requirements necessary to preserve and advance universal service, protect the public safety and welfare, ensure the continued quality of telecommunications services, and safeguard the rights of consumers.

(c) STATE AND LOCAL GOVERNMENT AUTHORITY. - Nothing in this section affects the authority of a State or local government to manage the public rights-of-way or to require fair and reasonable compensation from telecommunications providers, on a competitively neutral and nondiscriminatory basis, for use of public rights-of-way on a nondiscriminatory

basis, if the compensation required is publicly disclosed by such government.

(d) PREEMPTION. - If, after notice and an opportunity for public comment the Commission determines that a State or local government has permitted or imposed any statute, regulation, or legal requirement that violates subsection (a) or (b), the Commission shall preempt the enforcement of such statute, regulation, or legal requirement to the extent necessary to correct such violation or inconsistency.

(e) COMMERCIAL MOBILE SERVICE PROVIDERS. - Nothing in this section shall affect the application of section 332(c)(3) to commercial mobile service providers.

(f) RURAL MARKETS. - It shall not be a violation of this section for a State to require a telecommunications carrier that seeks to provide telephone exchange service or exchange access in a service area served by a rural telephone company to meet the requirements in section 214(e)(1) for designation as an eligible telecommunications carrier for that area before being permitted to provide such service. This subsection shall not apply-

(1) to a service area served by a rural telephone company that has obtained an exemption, suspension, or modification of section 251(c)(4) that effectively prevents a competitor from meeting the requirements of section 214(e)(1); and

(2) to a provider of commercial mobile services.

47 U.S.C. § 254 UNIVERSAL SERVICE.

(a) PROCEDURES TO REVIEW UNIVERSAL SERVICE REQUIREMENTS. -

(1) FEDERAL-STATE JOINT BOARD ON UNIVERSAL SERVICE. - Within one month after the date of enactment of the Telecommunications Act of 1996, the Commission shall institute and refer to a Federal-State Joint Board under section 410(c) a proceeding to

recommend changes to any of its regulations in order to implement sections 214(e) and this section, including the definition of the services that are supported by Federal universal support mechanisms and a specific timetable for completion of such recommendations. In addition to the members of the Joint Board required under section 410(c), one member of such Joint Board shall be a State-appointed utility consumer advocate nominated by a national organization of State utility consumer advocates. The Joint Board shall, after notice and opportunity for public comment, make its recommendations to the Commission 9 months after the date of enactment of the Telecommunications Act of 1996.

(2) COMMISSION ACTION. - The Commission shall initiate a single proceeding to implement the recommendations from the Joint Board required by paragraph (1) and shall complete such proceeding within 15 months after the date of enactment of the Telecommunications Act of 1996. The rules established by such proceeding shall include a definition of the services that are supported by Federal universal service support mechanisms and a specific timetable for implementation. Thereafter, the Commission shall complete any proceeding to implement subsequent recommendations from any Joint Board on universal service within one year after receiving such recommendations.

(b) UNIVERSAL SERVICE PRINCIPLES. - The Joint Board and the Commission shall base policies for the preservation and advancement of universal service on the following principles:

(1) QUALITY AND RATES. - Quality service should be available at just, reasonable, and affordable rates.

(2) ACCESS TO ADVANCED SERVICES. - Access to advanced telecommunications and information services should be provided in all regions of the Nation.

(3) ACCESS IN RURAL AND HIGH COST AREAS. - Consumers in all regions of the Nation, including low-income consumers and those in rural, insular, and high cost areas, should have access to telecommunications and information services, including interexchange services and advanced telecommunications and information services, that are reasonably comparable to those services provided in urban areas and that are available at rates that are reasonably comparable to rates charged for similar services in urban areas.

(4) EQUITABLE AND NONDISCRIMINATORY CONTRIBUTIONS. - All providers of telecommunications services should make an equitable and nondiscriminatory contribution to the preservation and advancement of universal service.

(5) SPECIFIC AND PREDICTABLE SUPPORT MECHANISMS. - There should be specific, predictable and sufficient Federal and State mechanisms to preserve and advance universal service.

(6) ACCESS TO ADVANCED TELECOMMUNICATIONS SERVICES FOR SCHOOLS, HEALTH CARE, AND LIBRARIES. - Elementary and secondary schools and classrooms, health care providers, and libraries should have access to advance telecommunications services as described in subsection (h).

(7) ADDITIONAL PRINCIPLES. - Such other principles as the Joint Board and the Commission determine are necessary and appropriate for the protection of the public interest, convenience, and necessity and are consistent with this Act.

(c) DEFINITION. -

(1) IN GENERAL. - Universal service is an evolving level of telecommunications services that the Commission shall establish periodically under this section, taking into account advances in telecommunications and information technologies and services. The Joint Board in recommending, and the Commission in establishing, the definition of the services that are supported by Federal universal service support mechanisms shall consider the extent to which such telecommunications services-

(A) are essential to education, public health, or public safety;

(B) have, through the operation of market choices by customers, been subscribed to by a substantial majority of residential customers;

(C) are being deployed in public telecommunications networks by telecommunications carriers; and

(D) are consistent with the public interest, convenience, and necessity.

(2) ALTERATIONS AND MODIFICATIONS. - The Joint Board may, from time to time, recommend to the Commission modifications in the definition of the services that are supported by Federal universal service support mechanisms.

(3) SPECIAL SERVICES. - In addition to the services included in the definition of universal service under paragraph (1), the Commission may designate additional services for such support mechanisms for schools, libraries, and health care providers for the purposes of subsection (h).

(d) TELECOMMUNICATIONS CARRIER CONTRIBUTION. - Every telecommunications carrier that provides interstate telecommunications services shall contribute, on an equitable and nondiscriminatory basis, to the specific, predictable, and

sufficient mechanisms established by the Commission to preserve and advance universal service. The Commission may exempt a carrier or class of carriers from this requirement if the carrier's telecommunications activities are limited to such an extent that the level of such carrier's contribution to the preservation and advancement of universal service would be de minimis. Any other provider of interstate telecommunications may be required to contribute to the preservation and advancement of universal service if the public interest so requires.

(e) UNIVERSAL SERVICE SUPPORT. - After the date on which Commission regulations implementing this section take effect, only an eligible telecommunications carrier designated under section 214(e) shall be eligible to receive specific Federal universal service support. A carrier that receives such support shall use that support only for the provision, maintenance, and upgrading of facilities and services for which the support is intended. Any such support should be explicit and sufficient to achieve the purposes of this section.

(f) STATE AUTHORITY. - A State may adopt regulations not inconsistent with the Commission's rules to preserve and advance universal service. Every telecommunications carrier that provides intrastate telecommunications services shall contribute, on an equitable and nondiscriminatory basis, in a manner determined by the State to the preservation and advancement of universal service in that State. A State may adopt regulations to provide for additional definitions and standards to preserve and advance universal service within that State only to the extent that such regulations adopt additional specific, predictable, and sufficient mechanisms to support such definitions or standards that do not rely on or burden Federal universal support mechanisms.

(g) INTEREXCHANGE AND INTERSTATE SERVICES. - Within 6 months after the date of enactment of the Telecommunications Act of 1996, the Commission shall adopt rules to require that the rates charged by providers of

interexchange telecommunications services to subscribers in rural and high cost areas shall be no higher than the rates charged by each such provider to its subscribers in urban areas. Such rules shall also require that a provider of interstate interexchange telecommunications services shall provide such services to its subscribers in each State at rates no higher than the rates charged to its subscribers in any other State.

(h) TELECOMMUNICATIONS SERVICES FOR CERTAIN PROVIDERS. -

(1) IN GENERAL

(A) HEALTH CARE PROVIDERS FOR RURAL AREAS. - A telecommunications carrier shall, upon receiving a bona fide request, provide telecommunications services which are necessary for the provision of health care services in a State, including instruction relating to such services, to any public or nonprofit health care provider that serves persons who reside in rural areas in that State at rates that are reasonably comparable to rates charged for similar services in urban areas in that State. A telecommunications carrier providing service under this paragraph shall be entitled to have an amount equal to the difference, if any, between the rates for services provided to health care providers for rural areas in a State and the rates for similar services provided to other customers in comparable rural areas in that State treated as a service obligation as a part of its obligation to participate in the mechanisms to preserve and advance universal service.

(B) EDUCATIONAL PROVIDERS AND LIBRARIES. - All telecommunications carriers serving a geographic area shall, upon a bona fide request for any of its services that are

within the definition of universal service under subsection (c)(3), provide such services to elementary schools, secondary schools, and libraries for educational purposes at rates less than the amounts charged for similar services to other parties. The discount shall be an amount that the Commission, with respect to interstate services, and the State, with respect to intrastate services, determine is appropriate and necessary to ensure affordable access to and use of such services by such entities. A telecommunications carrier providing service under this paragraph shall -

(i) have an amount equal to the amount of the discount treated as an offset to its obligation to contribute to the mechanisms to preserve and advance universal service, or

(ii) notwithstanding the provisions of subsection (e) of this section, receive reimbursement utilizing the support mechanisms to preserve and advance universal service.

(2) ADVANCED SERVICES. - The Commission shall establish competitively neutral rules-

(A) to enhance, to the extent technically feasible and economically reasonable, access to advanced telecommunications and information services for all public and nonprofit elementary and secondary school classrooms, health care providers, and libraries; and

(B) to define the circumstances under which a telecommunications carrier may be required to connect its network to such public institutional telecommunications users.

(3) TERMS AND CONDITIONS.- Telecommunications services and network capacity provided to a public institutional telecommunications user under this subsection may not be sold, resold, or otherwise transferred by such user in consideration for money or any other thing of value.

(4) ELIGIBILITY OF USERS. - No entity listed in this subsection shall be entitled to preferential rates or treatment as required by this subsection, if such entity operates as a for-profit business, is a school described in paragraph (5)(A) with an endowment of more than $50,000,000, or is a library not eligible for participation in State-based plans for funds under title III of the Library Services and Construction Act (20 U.S.C. 335c et seq.).

(5) DEFINITIONS.- For purposes of this subsection:

(A) ELEMENTARY AND SECONDARY SCHOOLS.- The term "elementary and secondary schools" means elementary schools and secondary schools, as defined in paragraphs (14) and (25), respectively, of section 14101 of the Elementary and Secondary Education Act of 1965 (20 U.S.C. 8801).

(B) HEALTH CARE PROVIDER.- The term "health care provider" means-

(i) post-secondary educational institutions offering health care instruction, teaching hospitals, and medical schools;

(ii) community health centers or health centers providing health care to migrants;

(iii) local health departments or agencies;

(iv) community mental health centers;

(v) not-for-profit hospitals

(vi) rural health clinics; and

(vii) consortia of health care providers consisting of one or more entities described in clauses (i) through (vi).

(C) PUBLIC INSTITUTIONAL TELECOMMUNICATIONS USER.- The term "public institutional telecommunications user" means an elementary or secondary school, a library, or a health care provider as those terms are defined in this paragraph.

(i) CONSUMER PROTECTION. - The Commission and the States should ensure that universal service is available at rates that are just, reasonable, and affordable.

(j) LIFELINE ASSISTANCE. - Nothing in this section shall affect the collection, distribution, or administration of the Lifeline Assistance Program provided for by the Commission under regulations set forth in section 69.117 of title 47, Code of Federal Regulations, and other related sections of such title.

(k) SUBSIDY OF COMPETITIVE SERVICES PROHIBITED. - A telecommunications carrier may not use services that are not competitive to subsidize services that are subject to competition. The Commission, with respect to interstate services, and the States, with respect to intrastate services, shall establish any necessary cost allocation rules, accounting safeguards, and the guidelines to ensure that services included in the definition of universal service bear no more than a reasonable share of the joint and common costs of facilities used to provide those services.